



This is a digital copy of a book that was preserved for generations on library shelves before it was carefully scanned by Google as part of a project to make the world's books discoverable online.

It has survived long enough for the copyright to expire and the book to enter the public domain. A public domain book is one that was never subject to copyright or whose legal copyright term has expired. Whether a book is in the public domain may vary country to country. Public domain books are our gateways to the past, representing a wealth of history, culture and knowledge that's often difficult to discover.

Marks, notations and other marginalia present in the original volume will appear in this file - a reminder of this book's long journey from the publisher to a library and finally to you.

Usage guidelines

Google is proud to partner with libraries to digitize public domain materials and make them widely accessible. Public domain books belong to the public and we are merely their custodians. Nevertheless, this work is expensive, so in order to keep providing this resource, we have taken steps to prevent abuse by commercial parties, including placing technical restrictions on automated querying.

We also ask that you:

- + *Make non-commercial use of the files* We designed Google Book Search for use by individuals, and we request that you use these files for personal, non-commercial purposes.
- + *Refrain from automated querying* Do not send automated queries of any sort to Google's system: If you are conducting research on machine translation, optical character recognition or other areas where access to a large amount of text is helpful, please contact us. We encourage the use of public domain materials for these purposes and may be able to help.
- + *Maintain attribution* The Google "watermark" you see on each file is essential for informing people about this project and helping them find additional materials through Google Book Search. Please do not remove it.
- + *Keep it legal* Whatever your use, remember that you are responsible for ensuring that what you are doing is legal. Do not assume that just because we believe a book is in the public domain for users in the United States, that the work is also in the public domain for users in other countries. Whether a book is still in copyright varies from country to country, and we can't offer guidance on whether any specific use of any specific book is allowed. Please do not assume that a book's appearance in Google Book Search means it can be used in any manner anywhere in the world. Copyright infringement liability can be quite severe.

About Google Book Search

Google's mission is to organize the world's information and to make it universally accessible and useful. Google Book Search helps readers discover the world's books while helping authors and publishers reach new audiences. You can search through the full text of this book on the web at <http://books.google.com/>



CT
BCZ
CCc

Avery J. Stone.
P.A.



CASES
ON
PRIVATE
CORPORATIONS

SELECTED AND ARRANGED

BY
GEORGE F. CANFIELD
Professor of Law, Columbia University

ASSISTED BY
I. MAURICE WORMSER
Assistant Professor of Law,
University of Illinois

INDIANAPOLIS
THE BOBBS-MERRILL COMPANY
PUBLISHERS

COPYRIGHT 1913
BY
THE BOBBS-MERRILL COMPANY.

PREFACE

For several years I have been intending to prepare a collection of cases on the law of private corporations, and when I learned that my former pupil, I. Maurice Wormser, now Assistant Professor of Law in the University of Illinois, had already entered upon a similar work, I concluded that a wise policy of conservation required that we combine our efforts.

Notwithstanding the enormous volume of legislation affecting corporations, which has been enacted during the past fifty years, there remains untouched a large number of common-law principles. These are fundamental—a firm grasp of them, indeed, is essential to a thorough knowledge not only of the common law but also the statutory law of corporations and this grasp can be only acquired by a critical study of the judicial decisions in which these common-law principles were developed and applied.

The present collection contains the more important of these decisions covering all the principal topics, and supplemented by notes of the editors, which, it is believed, will be useful to the student both during his period of study and during his professional career. The object of these notes is, first, to indicate the weight and general trend of authority upon important topics and disputed points; secondly, to facilitate independent research and special study of these topics and disputed points, and, thirdly, these notes have enabled us to reserve the entire body of the text for the important cases and those which, in the opinion of the editors, are best adapted to serve as a basis for analysis and discussion in the class-room.

It gives me great pleasure to acknowledge my indebtedness to my associate, Professor Wormser, for his painstaking and intelligent work in connection with the preparation of the notes and his helpful criticisms and suggestions with respect to the selection and classification of the cases.

GEORGE F. CANFIELD.

Columbia University, September 9th, 1912.

TABLE OF CONTENTS.

CHAPTER I.

THE LEGAL CONCEPTION OF A CORPORATION.

SECTION.	PAGE.
1. Considered in its relation to non-members.....	1
2. Considered in its relation to the state.....	67
3. Considered with respect to the question of residence or citizenship....	78
4. The corporation as distinguished from a joint-stock association.....	86
5. Considered in relation to its members. The distinction between capital stock and shares of stock.....	106

CHAPTER II.

CORPORATIONS DE JURE.

1. Under special acts or general laws.....	114
2. Corporations of two or more states.....	132

CHAPTER III.

CORPORATIONS DE FACTO.....	149
----------------------------	-----

CHAPTER IV.

POWERS OF A CORPORATION.

1. In general	196
2. To acquire its own shares, or those of other corporations.....	209
3. To enter into a co-partnership.....	218
4. To alienate all its property.....	224
Note on implied powers.....	229

CHAPTER V.

RIGHTS AND LIABILITIES ARISING OUT OF ULTRA VIRES TRANSACTIONS AS BETWEEN A CORPORATION AND NON-MEMBERS.

1. Ultra vires acquisition of property.....	234
2. Ultra vires transfer of property.....	264
3. Ultra vires contracts.....	275
4. Ultra vires torts.....	346

CHAPTER VI.

SUBSCRIBERS. SUBSCRIPTIONS TO STOCK.

1. Subscriber as distinguished from stockholder.....	354
2. Requisites of validity—Defenses	369

TABLE OF CONTENTS.

CHAPTER VII.

DIRECTORS.

SECTION.	PAGE.
1. Powers—Stockholders' control	422
2. Rights	450
A. Compensation	450
B. Indemnity	454
3. Duties	459
A. Obedience—Actions ultra vires.....	459
B. Diligence	471
C. Loyalty	491
4. Relation to stockholders individually.....	510

CHAPTER VIII.

STOCKHOLDERS.

1. Right to vote—The voting trust.....	520
2. By-laws	539
3. Dividends	548
4. Right to subscribe to new stock.....	579
5. Right to inspection of corporate books and records.....	592
6. Preferred stock	598
7. Over-issue of stock. Watered stock.....	619
8. Stockholders' right to sue on behalf of the corporation or on their own behalf. Powers of the majority.....	640
9. Transfer of stock.....	726

CHAPTER IX.

CREDITORS.

1. Relation between creditor and corporation. The trust fund theory....	780
2. Relation between creditor and director.....	801
A. At common law.....	801
B. By statute—The statutory liability of directors to creditors.	816
3. Relation between creditor and stockholder.....	823
A. At Common law. Trust fund theory.....	823
(1) Rights of creditors with respect to unpaid sub- scriptions	823
(2) Rights of creditors against holders of stock issued for money at less than par.....	830
(3) Rights of creditors against holders of stock issued for property at an over-valuation.....	850
B. By statute—The statutory liability of stockholders to cred- itors	858
4. Who is liable as stockholder? Effect of transfer of shares.....	882

CHAPTER X.

PROMOTERS. UNDERWRITING.....	903
------------------------------	-----

CHAPTER XI.

DISSOLUTION	940
-------------------	-----

TABLE OF CASES REPORTED.

[References are to Pages.]

A		
Aberdeen Railway Co. v. Blaikie Brothers, 1 Macqueen's App. Cas. 461	491	Bigelow v. Calumet &c. Mining Co., 155 Fed. 869 701
Allman v. Havana &c. R. Co., 88 Ill. 521	388	Bligh v. Brent, 2 Y. & C. Ex. 268 106
Almada & Tiritto Co., In re, L. R. 38 Ch. Div. 415	622	Board of Commissioners v. Reynolds, 44 Ind. 509 510
Ames v. Heslet, 19 Mont. 188	793	Booth v. Robinson, 55 Md. 419 499
Andrews v. Gas Meter Co., L. R. (1897) 1 Ch. Div. 361	598	Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49 941
Appleton v. Citizens' Central Nat. Bank, 190 N. Y. 417	322	Bowman Dairy Co. v. Mooney, 41 Mo. App. 665 290
Asiatic Banking Corporation, In re L. R. 4 Ch. App. Cas. 252	215	Briggs v. Spaulding, 141 U. S. 132 477
Ashbury Railway Carriage and Iron Co. v. Riche, L. R. 7 House of Lords 653	278	British Seamless Paper Box Co., In re, L. R. 17 Ch. Div. 467 903
Attorney-General v. McArthur, 38 Mich. 204	119	Brooklyn, Winfield &c. R. Co., Matter of, 75 N. Y. 335 946
Attorney-General v. Mersey Railway Co., L. R. (1907) 1 Ch. Div. 81, L. R. (1907) A. C. 415	196	Building & Loan Assn. of Dakota v. Chamberlain, 4 S. Dak. 271 172
Automatic &c. Syndicate Co., Ltd. v. Cunninghame, L. R. (1906) 2 Ch. Div. 34	428	Burr v. Wilcox, 22 N. Y. 551 356
Avon Springs Sanitarium Co. v. Weed, 119 App. Div. (N. Y.) 560, 189 N. Y. 557	370	Butchers' & Drovers' Bank of St. Louis v. McDonald, 130 Mass. 264 182
B		C
Bahia & San Francisco R. Co., Ltd., In re, L. R. 3 Q. B. Cas. 584	770	Caley v. Philadelphia &c. R. Co., 80 Pa. St. 363 398
Baltimore &c. R. Co. v. Hambleton, 77 Md. 341	364	Camden & Atlantic R. R. Co. v. Elkins, 37 N. J. Eq. 273 520
Barrett v. King, 181 Mass. 476	726	Capps v. Hastings Prospecting Co., 40 Neb. 470 384
Bartlett v. Drew, 57 N. Y. 587	785	Carlton, State on Information of, v. Dawson, 22 Ind. 272 114
Bath v. Standard Land Co., Ltd., (1911) 1 Ch. Div. 618	801	Cassidy v. Uhlmann, 170 N. Y. 505 806
Bathe v. Decatur County Agriculture Society, 73 Iowa 11	346	Central of Georgia Co. v. Union &c. R. Co., 144 Ala. 639 182
Bath Gas Light Co. v. Claffy, 151 N. Y. 24	314	Central Transportation Co. v. Pullman's Palace Car Co., 139 U. S. 24 295
Beach v. Miller, 130 Ill. 162	810	Charitable Corporation v. Sutton, 2 Atk. 400 471
Bergeron v. Hobbs, 96 Wis. 641	150	Cheaney v. Lafayette &c. R. Co., 68 Ill. 570 450
		Chemical National Bank v. Colwell, 132 N. Y. 250 745

[References are to Pages.]

Chetlain v. Republic Life Ins. Co., 86 Ill. 220	414	Erickson v. Revere Elevator Co., 110 Minn. 443	2
Chicago &c. R. Co. v. President &c. of Marseilles, 84 Ill. 643	209	F	
Chicago Hansom Cab Co. v. Yerkes, 141 Ill. 320	710	Fairtitle v. Gilbert, 2 Term Rep. (D. & E.) 169	264
Christensen v. Eno, 106 N. Y. 97	830	Farmers' Bank of Vine Grove v. Smith, 105 Ky. 816	929
Christopher v. Norvell, 201 U. S. 216	858	Farrington v. Putnam, 90 Maine 405	246
Cincinnati &c. R. Co. v. Danville &c. R. Co., 75 Ill. 113	179	Fietsam v. Hay, 122 Ill. 293	75
Citizens' Central Nat. Bank v. Appleton, 216 U. S. 196	322	Flint v. Pierce, 99 Mass. 68	541
Clark v. American Cannel Coal Co., 165 Ind. 213	176	Ford v. Easthampton Rubber Thread Co., 158 Mass. 84	567
Clark v. Turner, 73 Ga. 1	619	Fort Edward &c. Plank Road Co. v. Payne, 15 N. Y. 583	396
Coit v. North Carolina Gold Amalgamating Co., 119 U. S. 343	850	Fort Payne Rolling Mill v. Hill, 174 Mass. 224	494
Commercial Nat. Bank v. Wein- hard, 192 U. S. 243	422	Foss v. Harbottle, 2 Hare 461	640
Commonwealth v. Crompton, 137 Pa. St. 138	736	Foster v. Moulton, 35 Minn. 458	193
v. Dalzell, 152 Pa. St. 217	522	v. New Trinidad Lake Asphalt Co., Ltd., L. R. (1901) 1 Ch. Div. 208	554
v. Smith, 10 Allen (92 Mass.) 448	266	Franklin Bank v. Commercial Bank, 36 Ohio St. 350	215
Continental Securities Co. v. Bel- mont, 206 N. Y. 7	666	Franklin Bridge Co. v. Wood, 14 Ga. 80	116
Converse v. United Shoe Machin- ery Co., 185 Mass. 422	698	G	
v. United Shoe Machinery Co., 209 Mass. 539	700	Garmany v. Lawton, 124 Ga. 876	441
Coppage, Receiver, v. Hutton, 124 Ind. 401	382	Gashwiler v. Willis, 33 Cal. 11	433
Corbett v. South Eastern &c. R. Co.'s &c., L. R. (1906) 2 Ch. Div. 12	283	Glengary &c. Mining Co. v. Boeh- mer, 28 Colo. 1	715
Coulter v. Robertson, 24 Miss.. 278	958	Gluckstein v. Barnes, L. R. (1900) A. C. 240	907
Curry v. Scott, 54 Pa. St. 270	579	Goodwin v. New York &c. R. Co., 124 Fed. 358	140
D		Gramophone and Typewriter, Ltd., v. Stanley, L. R. (1906) 2 K. B. 856, L. R. (1908) 2 K. B. 89	39
Dartmouth College v. Woodward, 4 Wheat. (U. S.) 518	67	Greensboro &c. Turnpike Co. v. Stratton, 120 Ind. 294	457
Doctor v. Harrington, 196 U. S. 579	81	H	
Donald v. American Smelting & Refining Co., 62 N. J. Eq. 729	634	Handley v. Stutz, 137 U. S. 366	788
Donovan v. Purtrell, 216 Ill. 629	33	Handley v. Stutz, 139 U. S. 417	834
E		Hannon v. Siegel-Cooper Co., 167 N. Y. 244	352
East Anglian R. Co. v. Eastern Counties R. Co., 11 Common Bench (2 J. Scott) 775	275	Harris v. Independence Gas Co., 76 Kansas 750	337
Edwards v. Warren Linoline & Gasoline Works, 168 Mass. 564	90	Hastings Corporation v. Letton, L. R. (1908) 1 K. B. 378	964
		Hatch v. Dana, 101 U. S. 205	823
		Hawes v. Oakland, 104 U. S. 450	647

[References are to Pages.]

Hearst v. Putnam Mining Co., 28 Utah 184	691	L	
Hebgen v. Koeffler, 97 Wis. 313	913	Landes v. Hart, 131 App. Div. (N. Y.): 6	508
Hibbs v. Brown, 190 N. Y. 167	94	Licensed &c. Trading Assn., L. R. 42 Ch. Div. 1	936
Higgins v. California Petroleum &c. Co., 147 Cal. 363	28	Liverpool Ins. Co. v. Massachu- setts, 10 Wall. (U. S.) 566	86
v. Illinois Trust & Savings Bank, 193 Ill. 394	901	Lockhart v. Van Alstyne, 31 Mich. 76	548
Hill v. Murphy, 212 Mass. 1	688	Long v. Geo. Pacific R. Co., 91 Ala. 519	326
Hodges v. New England Screw Co., 1 R. I. 312	459	Louisville &c. R. Co. v. Letson, 2 How. (U. S.) 497	78
Hollins v. Brierfield Coal & Iron Co., 150 U. S. 371	789		
Home Fire Ins. Co. v. Barber, 67 Neb. 644	673	M	
Hopper v. Sage, 112 N. Y. 530	571		
Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174	842	McDonald v. Dewey, 202 U. S. 510	886
Howard, Receiver, v. Turner, 155 Pa. St. 349	828	v. Williams, 174 U. S. 397	795
Hubbard v. Worcester Art Mu- seum, 194 Mass. 280	258	McNeil v. The Tenth National Bank, 46 N. Y. 325	757
Hudson Real Estate Co. v. Tower, 156 Mass. 82	369	Madison Ave. Bap. Church v. Baptist Church in Oliver Street, 73 N. Y. 82	268
Hughes v. Antietam Mfg. Co., 34 Md. 316	391	Mallory v. Hanaur Oil Works, 86 Tenn. 598	218
Huntington v. Attrill, 146 U. S. 657	816	Maryland Trust Co. v. National Mechanics Bank, 102 Md. 608	212
Hunt, Receiver, v. O'Shea, As- signee, 69 N. H. 600	566	Menier v. Hooper's Telegraph Works, L. R. 9 Ch. App. Cas. 350	704
I		Merchants' Nat. Bank v. Wehr- mann, 202 U. S. 295	243
Ireland v. Globe Milling & Re- duction Co., 19 R. I. 180, 21 R. I. 9	544	Methodist &c. Church v. Pickett, 19 N. Y. 482	149
J		Mills v. Northern Railway &c. Co., L. R. 5 Chan. App. Cas. 621	799
Jacksonville &c. Railway & Navi- gation Co. v. Hooper, 160 U. S. 514	205	Miners' Ditch Co. v. Zellerbach, 37 Cal. 543	274
John V. Farwell Co. v. Wolf, 96 Wis. 10	239	Montgomery v. Forbes, 148 Mass. 249	168
K		Montgomery Web Co. v. Dienelt, 133 Pa. St. 585	24
Kenosha &c. R. Co. v. Marsh, 17 Wis. 13	416	Morrow v. Iron & Steel Co., 87 Tenn. 262	628
Kent v. Quicksilver Mining Co., 78 N. Y. 159	602	Mt. Sterling Coal Road Co. v. Little, 14 Bush (Ky.) 429	354
Kerfoot v. Farmers' & Mer- chants' Bank, 218 U. S. 281	237	N	
King v. Paterson & Hudson River R. Co., 29 N. J. L. 504	563	Nappanee Canning Co. v. Reid, Murdoch & Co., 159 Ind. 614	812
Krickerbocker Trust Co. v. Ise- lm, 185 N. Y. 54	878	Nassau Bank v. Jones, 95 N. Y. 115	286
Kreissl v. Distilling Co. of Amer- ica, 61 N. J. Eq. 5	531	National Bank v. Matthews, 98 U. S. 621	305

[References are to Pages.]

National Financial Co., In re, L. R. 3 Ch. App. Cas. 791	454	Risdon Iron & Locomotive Works v. Furness, L. R. (1906) 1 K. B. 49	869
National Home Bldg. & Loan Assn. v. Home Savings Bank, 181 Ill. 35	300	Rockford &c. R. Co. v. Sage, 65 Ill. 328	927
Nebraska Chicory Co. v. Lednický, 79 Neb. 587	377	Rogers v. Nashville &c. R. Co., 91 Fed. 299	655
Newcomb-Endicott Co. v. Fee, 167 Mich. 574	161	Rountree v. Adams Express Co., 165 Fed. 152	93
New York Central &c. R. Co. v. United States, 212 U. S. 481	16	Russell v. American Bell Tel. Co., 180 Mass. 467	766
New York & New Haven R. Co. v. Schuyler, 34 N. Y. 30	739	S	
Nims v. Mount Hermon Boy's School, 160 Mass. 177	347	St. Louis &c. R. Co. v. Terre Haute &c. R. Co., 145 U. S. 393	328
North Milwaukee Town Site Co. v. Bishop, 103 Wis. 492	539	St. Peter's R. C. Congregation v. Germain, 104 Ill. 440	234
Norwich Lock Mfg. Co. v. Hockaday, 89 Va. 557	408	Sawyer v. Hoag, 17 Wall. (U. S.) 610	780
O		Schnittger v. Old Home &c. Min. Co., 144 Cal. 603	496
Ohio Valley National Bank v. Hulitt, 204 U. S. 162	882	Scollans v. Rollins, 179 Mass. 346	763
Old Dominion Copper &c. Smelting Co. v. Lewisohn, 210 U. S. 206	920	Scott v. Baltimore & Ohio R. Co., 93 Md. 475	612
P		v. Pequonnock National Bank, 15 Fed. 494	752
Patch v. Wabash Railroad Co., 207 U. S. 277	146	Seymour v. Spring Forest Cemetery Assn., 144 N. Y. 333	505
People v. Coleman, 126 N. Y. 433	109	Sheffield Corporation v. Barclay, L. R. (1905) A. C. 392	772
v. Moss, 187 N. Y. 410	464	Smith v. San Francisco &c. R. Co., 115 Cal. 584	523
v. Powell, 201 N. Y. 194	445	Society Perun v. Cleveland, 43 Ohio St. 481	184
v. Whalen, 119 App. Div. (N. Y.) 749	224	State v. Southern Building & Loan Assn., 132 Ala. 50	948
People's Pleasure Park Co. v. Rohleder, 109 Va. 439	3	v. Standard Oil Co., 49 Ohio St. 137	52
Pinney v. Nelson, 183 U. S. 144	865	State Trust Co. v. Turner, 111 Iowa 664	853
Pollitz v. Gould, 202 N. Y. 11	676	Stein v. Howard, 65 Cal. 616	625
Price v. Holcomb, 89 Iowa 123	707	Stevens v. Episcopal Church History Co., 140 App. Div. (N. Y.) 570	167
Pullman's Palace Car Co. v. Central Transportation Co., 171 U. S. 138	332	Stokes v. Continental Trust Co., 186 N. Y. 285	581
Q		Strong v. Repide, 213 U. S. 419	515
Quincy Railroad Bridge Co. v. County of Adams, 88 Ill. 615	132	Sturgis v. Vanderbilt, 73 N. Y. 384	956
R		Swan Land & Cattle Co. v. Frank, 148 U. S. 603	944
Rabe v. Dunlap, 51 N. J. Eq. 40	680	T	
Railroad v. Barnhill, 91 Tenn. 395	137	Telegraph v. Loetscher, 127 Iowa 383	916
Raynolds v. Diamond Mills Paper Co., 69 N. J. Eq. 299	574	Third Nat. Bank v. Buffalo German Ins. Co., 193 U. S. 581	730
Rieger, Kapner & Altmark, In re, 157 Fed. 609	46		

[References are to Pages.]

		W	
Tompkinson v. South-Eastern R. Co., L. R. 35 Ch. Div. 675	697	Waukon & Mississippi R. Co. v. Dwyer, 49 Iowa 121	360
Towers v. African Tug Co., L. R. (1904) 1 Ch. Div. 558	684	Webb v. Baltimore &c. R. Co., 77 Md. 92	405
Treadwell v. Salisbury Mfg. Co., 7 Gray (73 Mass.) 393	227	Webster v. Upton, 91 U. S. 65	749
Trustees of Dartmouth College v. Woodward, 4 Wheat (U. S.) 518	67	Wells Co. v. Gastonia Cotton Mfg. Co., 198 U. S. 177	124
Tuttle v. George A. Tuttle Co., 101 Maine 287	932	Wendover Athletic Association, In re, 70 Misc. (N. Y.) 273	122
Twin-Lick Oil Co. v. Marbury, 91 U. S. 587	502	Werner v. Hearst, 177 N. Y. 63	14
U		Wheeler v. Abilene Nat. Bank Bldg. Co., 159 Fed. 391	722
		v. Pullman Iron & Steel Co., 142 Ill. 197	951
United States v. Lehigh Valley R. Co., 220 U. S. 257	59	White v. Salisbury, 33 Mo. 150	735
v. New York Herald Co., 159 Fed. 296	22	White, Corbin & Co. v. Jones, 167 N. Y. 158	898
V		White Mountains R. Co. v. Eastman, 34 N. H. 124	402
Vance v. Erie Railroad Co., 32 N. J. L. 334	11	Whitman v. Oxford National Bank, 176 U. S. 559	873
Varney v. Baker, 194 Mass. 239	592	Whitney Arms Co. v. Barlow, 63 N. Y. 62	310
Venner v. Chicago City Railway Co., 246 Ill. 170	594	Williams v. Western Union Telegraph Co., 93 N. Y. 162	557
Visalia Gas &c. Light Co. v. Sims, 104 Cal. 326	319	Wilson v. Carter Oil Co., 46 W. Va. 469	222
		v. Leary, 120 N. Car. 90	953
		Windmuller v. Standard Distilling Co., 114 Fed. 491	717
		Wood v. Hammond, 16 R. I. 98	255

TABLE OF CASES CITED.

[References are to Pages.]

A		Armstrong v. Karshner, 47 Ohio St.	276	408, 416
Aaron's Reefs v. Twiss, L. R. (1896)	921	Ashley's Case, L. R. 9 Eq. 263		421
App. Cas. 273		Ashtabula & C. R. Co. v. Smith, 15 Ohio		384
Abbot v. American Hard Rubber Co.,	227	St. 328		
33 Barb. (N. Y.) 578		Ashton v. Burbank, 2 Dill C. C. (U.		413
Abbot v. Omaha & Refining Co., 4	167	S.) 335		698
Nehr. 416		v. Dashaway Assn., 84 Cal. 61		370
Aberdeen R. R. Co. v. Blaikie, 1 Macq.	494	Ashuelot Boot & Shoe Co. v. Hoyt, 56		121
H. L. Cas. 461		N. H. 548		
Abrah v. N. E. Ry., 11 App. Cas. 247	14	Aspen Water and Light Co. v. City of		121
Adams v. Burke, 201 Ill. 395	499	Aspen, 5 Colo. App. 12		
Advance Thrasher Co. v. Rockafellow,	239	Asphalt Const. Co. v. Bouker, 135 N.		509
16 S. Dak. 462		Y. S. 134		
Agua Fria Copper Co. v. Bashford & C.	175	Assets Collecting Co. v. Barnes-King		785
4, 4 Ariz. 203		Development Co., 198 Fed. 82		
Aldine Mig. Co. v. Phillips, 129 Mich.	501	Assignment of Mutual & C. Ins. Co., In		300
240		re, 107 Iowa 143		
Alexander v. Atlanta & C. R. Co., 113	699	Athol Music Hall Co. v. Carey, 116		737
Ga. 193		Mass. 471		
v. Automatic Tel. Co., L. R. (1900)		Atkinson v. Foster, 134 Ill. 472		370
2 Ch. Div. 56	647	v. Marietta R. Co., 15 Ohio St. 21		184
v. Relfe, 74 Mo. 495	347	Atlanta v. Gate City & C. Co., 71 Ga.		115
v. Searcy, 81 Ga. 536	684	106		
v. Tolleston Club, 110 Ill. 65	237	Atlantic R. Co. v. Sullivant, 5 Ohio St.		184
Allemong v. Simmons, 124 Ind. 199	10	276		
Allen v. Curtis, 26 Conn. 456	514	Atlas Tack Co. v. Macon Hardware		812
v. South Boston R. Co., 150 Mass.	744, 745	Co., 101 Ga. 391		
200		Attala Iron Ore Co. v. Virginia & C.		494
v. Woonsocket Co., 11 R. I. 288	224	Coke Co., 111 Tenn. 527		
Allison v. Southern Ry. Co., 129 N. C.	146	Attorney-General for Canada v. Stand-		926
336		ard Trust Co., (1911) A. C. 498		
Althaus v. Richardson Gas & Oil Co.,	793	Attorney-General v. Great Eastern R.		205
81 Kana. 717		Co., 5 App. Cas. 473		
Amrose Lake & C. Min. Co., In re, L.	907	v. Great Northern Ry. Co., 1 Drew.		39
R. 14 Ch. Div. 390		& S. 154		
American Exchange Nat. Bank v.	770	Auburn Bolt & C. Works v. Shultz, 143		413
Woodlawn Cemetery, 194 N. Y. 116		Pa. St. 256		
American Ice & Industries Co. v. Crane,	698	Auburn Button Co. v. Sylvester, 68		945
142 Ala. 620		Hun (N. Y.) 401		
American Salt Co. v. Heidensheimer,	167	Aurora & Horticultural Society v. Pad-		231
80 Tex. 344		dock, 80 Ill. 263		
American Tube & Iron Co. v. Baden	853	Avon Springs Sanitarium Co. v. Kel-		377
Gas Co., 165 Pa. St. 489		logg, 189 N. Y. 557		
American Tube-Works v. Boston Ma-	622	v. Kellogg, 125 App. Div. (N. Y.)		377
chine Co., 139 Mass. 5		51		
Amer. v. Amer. Telephone & Telegraph	701			
Co., 166 Fed. 820		B		
Anderson's Case, L. R. 7 Ch. Div. 75	852	Babcock v. Farwell, 245 Ill. 14		676
Anderson v. Nicholas, 28 N. Y. 600	769	Badger Paper Co. v. Rose, 95 Wis. 145		370
v. Thompson, 51 La. Ann. 727	195	Bagley v. Carthage & C. R. Co., 165 N.		454
v. W. G. Dyer & Bros., 94 Minn.	578	Y. 179		
30		Bagshaw v. Eastern & C. R. Co., 7 Hare		647
Andover & C. Turnpike Co. v. Gould, 6	396	114		
Mass. 40		Bahia & San Francisco R. Co., In re,		779
Andres v. Morgan, 62 Ohio St. 236	28, 59	L. R. 3 Q. B. 584		
Andrews Bros. Co. v. Youngstown Coke	90	Baker's Appeal, 109 Pa. St. 461		428
Co., 86 Fed. 585		Baldwin v. Canfield, 26 Minn. 43		111
Anthony v. American Glucose Co., 146	59	v. Chicago & C. R. Co., 86 Fed. 167		146
N. Y. 407		Balkis Consolidated Co. v. Tompkin-		779
v. Household Sewing Machine Co.,	602	son, (1893) A. C. 403		
16 R. I. 571		Baltimore & C. R. Co. v. Fifth Baptist		182
Arthorpe v. Peter Schoenhofen Brewing	46	Church, 137 U. S. 568		
Co., 80 L. T. 395		Baltimore Retort & Fire Brick Co. v.		738
Arkansas & C. Canal Co. v. Farmers'		Mail, 65 Md. 93		
Loan & C. Co., 13 Colo. 587	59, 628			

B

[References are to Pages.]

Banet v. Alton &c. R. Co., 13 Ill. 504	413	Bjorngaard v. Goodhue County Bank, 49 Minn. 483	521, 665, 715
Bangor &c. Slab Co., In re, L. R. 20 Eq. Cas. 59	619	Blair v. City of Chicago, 201 U. S. 400	239
Bangor Electric Light & Power Co. v. Robinson, 52 Fed. 520	769	Blinn v. Riggs, 110 Ill. App. 37	521
Banigan v. Bard, 134 U. S. 291	611	Bloede Co. v. Bloede, 84 Md. 129	729
Bank v. Bank, 92 U. S. 128	218	Blodgett v. Morrill, 20 Vt. 509	406
v. Bank of Victoria, L. R. 3 Pr. Coun. App. Cas. 526	243	Blum v. Whitney, 185 N. Y. 232	927
Bank of Augusta v. Earle, 13 Pet. (U. S.) 519	3	Blyth's Case, L. R. 4 Ch. Div. 140	360
Bank of Columbia v. Patterson's Admr., 7 Cranch (U. S.) 299	230	Board of Commissioners v. Reynolds, 44 Ind. 509	518
Bank of Mississippi v. Duncan, 56 Miss. 166	964	Board v. Mississippi &c. R. Co., 21 Ill. 337	413
Bank of Montreal v. Potts Salt and Lumber Co., 90 Mich. 345	794, 815	Boatmen's Ins. & Trust Co. v. Able, 48 Mo. 136	735
Bank of United States v. Dandridge, 12 Wheat. (U. S.) 64	230	Boldenweck v. Bullis, 40 Colo. 253	676
Barnes v. Black &c. Coal Co., 101 Tenn. 354	544	Bonaparte v. Baltimore &c. R. Co., 75 Md. 340	115
v. Suddard, 117 Ill. 237	237	Bond v. Bean, 72 N. H. 444	738
Barron v. Burrill, 86 Maine 66	360	Bond v. Terrell Cotton &c. Mfg. Co., 82 Tex. 309	313
Barrow v. Faringa Mines, 2 Ch. Div. 658	939	Boogher v. Life Assn., 75 Mo. 319	13
Barstow v. Savage Mining Co., 64 Cal. 388	769	Booth v. Bunce, 33 N. Y. 139	28
Bartholomew v. Derby Rubber Co., 69 Conn. 521	229	v. Campbell, 37 Md. 522	368
Bassett v. Fairchild, 132 Cal. 637	454	v. Robinson, 55 Md. 419	215
Bateman v. Mid-Wales R. Co., L. R. 1 C. P. 499	231	v. Wonderly, 36 N. J. L. 250	171
Bates v. Coronado Beach Co., 109 Cal. 160	225	Borland's Trustee v. Steel Bros. & Co., Ltd., L. R. (1901) 1 Ch. Div. 279	729
Bawden v. Taylor, 254 Ill. 464	514	Boston & Albany R. Co. v. Richardson, 135 Mass. 473	779
Beach v. First M. E. Church, 96 Ill. 177	371	Botwick v. Young, 118 App. Div. (N. Y.) 490	852
v. Miller, 130 Ill. 162	505	Bouton v. Dement, 123 Ill. 142	397
v. Wakefield, 107 Iowa 567	309	Boyd v. American Carbon Black Co., 182 Pa. St. 206	224
Beaconsfield Heights Estate Co., In re, 22 Vict. Law Rep. 97	428	v. Peach Bottom R. Co., 90 Pa. St. 169	384, 402
Beales v. Buffalo &c. Construction Co., 49 App. Div. (N. Y.) 589	360	Boynton v. Andrews, 63 N. Y. 93	858
Beatty v. North-West Transportation Co., L. R. 12 App. Cas. 589	715	Bradbury v. Boston Canoe Club, 153 Mass. 77	231
Bedford R. Co. v. Bower, 48 Pa. St. 29	397, 402	Bradley v. Ballard, 55 Ill. 413	313
Beers v. Bridgeport Spring Co., 42 Conn. 17	571	v. Reppell, 133 Mo. 545	176, 958
Belfast &c. R. Co. v. Belfast, 77 Maine 445	554	Brady v. Delaware Ins. Co., 2 Penn. (Del.) 237	176
v. Moore, 60 Maine 561	396	Braintree Water Co. v. Braintree, 146 Mass. 482	132
Belleville v. Citizens' Horse R. Co., 152 Ill. 171	948	Brandenstein v. Hope, 101 Cal. 136	175
Bellona Co. Case, 3 Bland (Md.) 442	11	Bray v. Farwell, 81 N. Y. 600	391
Belton, Matter of, 47 La. Ann. 1614	11	Breeze v. Lone &c. Mining Co., 39 Wash. 602	689
Bennett v. Minott, 28 Ore. 339	28	Breinig v. Sparrow, 39 Ind. App. 455	224
Benton v. City of Elizabeth, 61 N. J. L. 411	239	Bremen Savings Bk. v. Branch &c. Saw Co., 104 Mo. 425	28
Bent v. Priest, 10 Mo. App. 543	509	Brewer v. Boston Theatre, 104 Mass. 378	665
Bent, Receiver, v. Underdown, 156 Ind. 516	842	v. State, 7 Lea (Tenn.) 682	193
Bergeron v. Hobbs, 96 Wis. 641	167	Bridges v. National Bank, 185 N. Y. 146	548
Bernheimer v. Converse, 206 U. S. 516	864	Briggs v. Cape Cod Canal Co., 137 Mass. 71	175
Bernier v. Grescom-Spencer Co., 161 Fed. 438	578	Brinkerhoff-Farris Trust Savings Co. v. Home Lumber Co., 118 Mo. 447	736
Beshoar v. Chappell, 6 Colo. App. 323	689	Brinkerhoff Zinc Co. v. Boyd, 192 Mo. 597	472
Best Brewing Co. v. Klassen, 185 Ill. 37	232, 300	Brinkley v. Hambleton, 67 Md. 169	752, 886
Beveridge v. N. Y. Elevated R. Co., 112 N. Y. 1	428, 441	Brisbane v. Delaware, L. & W. R. Co., 94 N. Y. 204	744
Rias v. Atkinson, 64 W. Va. 486	707	Broderip v. Salomon, L. R. 2 Ch. 323	46
Biddle v. Bayard, 14 Pa. St. 150	769	Brokaw v. New Jersey R. &c. Co., 32 N. J. L. 328	348
Bigelow v. Gregory, 73 Ill. 197	167	Bronson Elec. Co. v. Rheubottom, 122 Mich. 608	548
Bishop v. American Preservers Co., 157 Ill. 284	221	Brooklyn Steam Transit Co. v. Brooklyn, 78 N. Y. 524	948
Bissell v. Michigan &c. R. Co., 22 N. Y. 258	353	Brown v. Allebach, 166 Fed. 488	830
		v. De Young, 167 Ill. 549	701
		v. Lehigh Coal & Navigation Co., 49 Pa. St. 270	563

[References are to Pages.]

Brown v. Winnisimmet Co., 11 Allen (Mass.) 326	209	Catskill Bank v. Gray, 14 Barb. (N. Y.) 471	224
Brigham v. Peter Bent Brigham Hospital, 126 Fed. 796	264	Central Mfg. Co. v. Montgomery, 144 Mo. App. 494	11
Bright v. Lord, 51 Ind. 272	573	Central R. Co. v. Pennsylvania R. Co., 31 N. J. Eq. 475	387
Brightman v. Bates, 175 Mass. 105	530	Central R. R. & Banking Co. v. Smith, 76 Ala. 572	347
Brundred v. Rice, 49 Ohio St. 640	66	Central Transportation Co. v. Pullman's Palace Car Co., 139 U. S. 24	231
Brunswick Gas Light Co. v. United Gas & Light Co., 85 Maine 532	231	Central Trust Co. v. Chattanooga & R. Co., 68 Fed. 685	140
Bryant's Pond Steam-Mill Co. v. Felt, 87 Maine 234	370, 371	v. Bridges, 57 Fed. 753	726
Bucksport &c. R. Co. v. Buck, 65 Maine 536	391	v. West India Improvement Co., 169 N. Y. 314	763
v. Buck, 68 Maine 81	399	Champion v. Memphis &c. R. Co., 35 Miss. 692	413
Buffalo &c. R. Co. v. Clark, 22 Hun (N. Y.) 359	382	Chandler v. Bacon, 30 Fed. 538	920
v. Dudley, 14 N. Y. 336	396, 421	Chapman v. Barney, 129 U. S. 677	94
v. Gifford, 87 N. Y. 294	370, 384	v. Bates, 61 N. J. Eq. 658	539
Buffalo Loan &c. Co. v. Medina Gas &c. Co., 162 N. Y. 67	11	v. Iron Clad Rheostat Co., 62 N. J. L. 497	211
Bullock v. Falmouth &c. Turnpike Co., 85 Ky. 184	355	Charlestown &c. Shoe Co. v. Dunsmore, 60 N. H. 85	440
Burden v. Burden, 159 N. Y. 287	239	Charlotte &c. R. Co. v. Blakely, 3 Stroth. (S. Car.) 245	360
Burke v. Smith, 16 Wall. (U. S.) 390	402	Chase v. Sycamore &c. R. Co., 38 Ill. 215	363
Burland v. Earle, L. R. (1902) A. C. 83	707, 715	Cheetham v. McCormick, 178 Pa. St. 186	639
Burroughs v. North Carolina R. Co., 67 N. Car. 376	573	Chesapeake & Ohio R. Co. v. Howard, 178 U. S. 153	353
Burr v. Wilcox, 22 N. Y. 551	360	Chesley v. Soo Lignite Coal Co., 19 N. Dak. 18	873
Burrows v. Interborough Metropolitan Co., 156 Fed. 389	684	Chewacla Lime Works v. Dismukes, 87 Ala. 344	233, 300
Bushnell v. Consolidated Ice Machine Co., 138 Ill. 67	195, 958	Chicago &c. R. Co. v. Auditor General, 53 Mich. 79	137
Butler v. Land & Mining Co., 139 Mo. 467	815	v. Union Pac. R. Co., 47 Fed. 15	444
Butler University v. Scoonover, 114 Ind. 381	359	Chicago v. Cameron, 120 Ill. 447	665, 684
Butternuts &c. Turnpike Co. v. North, 1 Hill (N. Y.) 518	398	Chicago City R. Co. v. Allerton, 18 Wall. (U. S.) 233	428
Byrne v. Schuyler &c. Mfg. Co., 65 Conn. 336	218, 698	Chicago Hansom Cab Co. v. Yerkes, 141 Ill. 320	451
C			
Caley v. Philadelphia &c. R. Co., 80 Pa. St. 363	416	Chicago Macaroni Mfg. Co. v. Boggiano, 202 Ill. 312	523
v. The Railroad Co., 30 P. F. Smith 367	402	Chicago Union T. Co. v. Chicago, 199 Ill. 579	39, 59
California National Bank v. Kennedy, 167 U. S. 362	218, 245	Christensen v. Eno, 106 N. Y. 97	634
California Southern Hotel Co. v. Calender, 94 Cal. 120	359	Christian &c. Grocery Co. v. Fruitdale Lumber Co., 121 Ala. 340	167, 168
Camden &c. R. Co. v. May's Landing &c. R. Co., 48 N. J. L. 530	313	Christian Union v. Yount, 101 U. S. 352	232
Camden &c. Trust Co. v. Citizens' &c. Storage Co., 69 N. J. Eq. 718	507	Citizen's Life Assn. Co. v. Brown, App. Cas. 423	14
Camden Nat. Bank v. Fries-Breslin Co., 214 Pa. St. 395	566	City Bank of Columbus v. Bruce, 17 N. Y. 507	211
Camden v. Stewart, 144 U. S. 104	859	Clapp v. Peterson, 104 Ill. 26	212
Campbell v. American Zylonite Co., 122 N. Y. 455	611	Clark v. American Coal Co., 86 Iowa 436	676
Cape Breton Co., In re, 29 Ch. Div. 795	913	v. Brown, 108 S. W. (Tex. Civ. App.) 421	428
Carey v. Savings Union, 22 Wall. (U. S.) 38	554	Clarke v. Lincoln Lumber Co., 59 Wis. 655	628
Carmichael's Case, 2 Ch. Div. 643	939	Clausen v. Head, 110 Wis. 405	167
Carpenter v. Danforth, 52 Barb. (N. Y.) 581	514	Cleveland Paper Co. v. Courier Co., 67 Mich. 152	224
Carrington v. Basshor Co., 84 Atl. (Md.) 746	490	Clews v. Friedman, 182 Mass. 555	757
Carson v. Iowa City Gaslight Co., 80 Iowa 638	698	Close v. Glenwood Cemetery, 107 U. S. 466	175
Cartwright v. Dickinson, 88 Tenn. 476	416	v. Potter, 155 N. Y. 145	864
Casnas v. Audubon Hotel Co., 124 La. 786	195	Coal &c. R. Co. v. Peabody Coal Co., 230 Ill. 164	10
Cass v. Kelly, 133 U. S. 21	294	Coats v. Donnell, 94 N. Y. 168	232
Castle Braid Co., In re 145 Fed. 224	211	Cochran v. Arnold, 58 Pa. St. 309	172
		v. Wiechers, 119 N. Y. 399	864
		Coffey v. Coffey, 179 Ill. 283	738
		Cohen v. Big Stone Co., 111 Va. 486	227

[References are to Pages.]

Colman v. Eastern Counties R. Co., 10 Beavan 1	230	Danville Seminary v. Mott, 136 Ill. 289	956
Colonial Bank v. Cady & Williams, L. R. 15 App. Cas. 267	763	Davenport v. Dows, 18 Wall. (U. S.) 626	673
Comanche Cotton Oil Co. v. Browne, (Tex. Civ. App.) rev'd, 99 Tex. 660	413	v. Lines, 72 Conn. 118	799
Commercial Bank v. Warthen, 119 Ga. 990	363	Davey v. Brooklyn & N. Y. Ferry Co., 196 N. Y. 99	822
Commercial Fire Ins. Co. v. Board of Revenue, 99 Ala. 1	218	Davis v. Memphis &c. R. Co., 87 Ala. 633	956
Common v. McArthur, 29 Can. Sup. Ct. 239	195	v. Old Colony Railroad Co., 131 Mass. 258	233
Commonwealth v. Bringham, 103 Pa. St. 134	531	v. Stevens, 104 Fed. 235	176
v. Monongahela Bridge Co., 216 Pa. St. 108	11	v. United States &c. Light Co., 77 Md. 35	218
v. New York &c. R. Co., 132 Pa. St. 591	108	Day v. Ogdensburgh &c. R. Co., 107 N. Y. 129	948
v. Phila. County, 193 Pa. St. 236	175	Deaderick v. Wilson, 8 Baxt. (67 Tenn.) 108	514
v. Smith, 10 Allen (Mass.) 448	78, 231	Deaton Grocery Co. v. International Harvester Co., 47 Tex. Civ. App. 267	322
Commonwealth S. S. Co. v. American Shipbuilding Co., 197 Fed. 797	926	Debnam v. Southern &c. Tel. Co., 126 N. Car. 831	146
Commonwealth v. Worcester, 3 Pick. 462	544	De Bussche v. Alt, L. R. 8 Ch. Div. 286	688
Conklin v. United States Shipbuilding Co., 140 Fed. 219	953	Decatur Mineral Land Co. v. Palm, 113 Ala. 531	665
Conover v. Hull, 10 Wash. 673	785	DeKoven v. Alsop, 205 Ill. 309	563, 574
Consort &c. Mines, In re 1 Ch. Div. 575	939	Delano v. Gardner Case, 121 Ill. 247	809
Continental Adjustment Co. v. Cook, 152 Fed. 652	834	Delavan v. N. Y., N. H. & H. R. Co., 137 N. Y. S. 207	704
Continental Ins. Co. v. New York &c. R. Co., 187 N. Y. 225	501, 673, 726	Delaware & Hudson Co. v. Albany &c. R. Co., 213 U. S. 435	655
Converse v. Sharpe, 161 N. Y. 571	812	Demarest v. Flack, 128 N. Y. 205	16, 171
Cook v. American Tubing &c. Co., 28 R. I. 41	233	De Neufville v. New York & N. R. Co., 81 Fed. 10	701
Co-operative Law Co., Matter of, 198 N. Y. 479	233	Densmore Oil Co. v. Densmore, 64 Pa. St. 43	920
Coppin v. Greenless & Ransom Co., 38 Ohio St. 275	214	Denver Fire Ins. Co. v. McClelland, 9 Colo. 11	314
Coquard v. National Linseed Oil Co., 171 Ill. 480	953	De Ruvigne's Case, L. R. 5 Ch. Div. 306	834
Corbus v. Alaska &c. Min. Co., 187 U. S. 455	655	Des Moines Gas Co. v. West, 50 Ia. 16	39
Cornford v. Carlton Bk., 1 Q. B. 392	13	Detroit &c. R. Co. v. Campbell, 140 Mich. 384	184
Corry v. Londonderry &c. R. Co., 29 Beav. 263	557	Detroit v. Dean, 106 U. S. 537	655
Corwith v. Culver, 49 Ill. 502	359, 406	De Witt County National Bank v. Michelberry, 244 Ill. 77	239
Cory v. Wadsworth, 118 Ala. 488	815	Diamond State Iron Co. v. Husbands, 68 Atl. (Del.) 240	956
Cottrell v. Albany Card and Paper Mfg. Co., 142 App. Div. (N. Y.) 148	785	Dickerman v. Northern Trust Co., 176 U. S. 181	920
Covington &c. R. Co. v. Bowler's Heirs, 9 Bush (Ky.) 468	505	Distilling & Cattle Feeding Co. v. People, 156 Ill. 448	59
Cowell v. Springs Co., 100 U. S. 55	232	Doctor v. Harrington, 196 U. S. 579	673
Coxe v. State, 144 N. Y. 396	175	Doe ex dem. Banks v. Booth, 2 Bos. & P. 219	266
Craig v. Andes, 93 N. Y. 405	398	Doherty v. Arkansas &c. R. Co., 142 Fed. 104	370
Cratty v. Peoria Law Library Assn., 219 Ill. 516	566, 578	v. Mercantile Trust Co., 184 Mass. 590	665
Cravens v. Eagle Cotton Mills Co., 120 Ind. 6	382	Dorris v. Sweeney, 60 N. Y. 463	387, 413
Crawford v. Roney, 126 Ga. 763	396	Doty v. First Nat. Bank, 3 N. Dak. 9	757
v. Roney, 130 Ga. 515	557	v. Patterson, 155 Ind. 60	167
Crichton v. Webb Press Co., 113 La. 167	578, 715, 726	Douglas v. Ireland, 73 N. Y. 100	858
Crowell v. Jackson, 53 N. J. L. 656	519	Dovey v. Cory, L. R. App. Cas. 477	477, 490
Cunningham v. German Ins. Bank, 101 Fed. 377	444	Downey v. Finucane, 205 N. Y. 251	920
Curran v. Arkansas, 15 How. (U. S.) 304	783	Downing v. Mt. Washington Road Co., 40 N. H. 230	205
Currie's Case, 3 De G. J. & T. 367	634, 833	Driscoll v. West &c. Mfg. Co., 59 N. Y. 96	548, 735
Curry v. Scott, 54 Pa. 270	611	Drummer v. Smedley, 110 Mich. 466	842
Curtin v. Salmon River &c. Co., 130 Cal. 345	499	Ducat v. City of Chicago, 48 Ill. 172	85
Curtis v. Leavitt, 15 N. Y. 64	209	Dunbar v. American Tel. &c. Co., 224 Ill. 9	59, 521
p		Duncomb v. New York &c. R. R. Co., 84 N. Y. 190	493
Danville &c. Trust Co. v. Parks, 88 Ill. 470	113	Dunphy v. Travelers' Newspaper Assn., 146 Mass. 495	665

TABLE OF CASES CITED.

xvii

[References are to Pages.]

Dupee v. Boston Water Power Co., 114 Mass. 37	211, 231	Finch v. Ullman, 105 Mo. 255	193
Durant v. Abendroth, 69 N. Y. 148	384	Finnegan v. Noerenberg, 52 Minn. 239	166
v. Kennett, L. R. 5 C. P. 262	109	First Ave. Land Co. v. Parker, 111 Wis. 1	772
Durkee v. People, 155 Ill. 354	523	First National Bank v. Holland, 99 Va. 495	738
Dykman v. Keeney, 160 N. Y. 677	799	v. National Exchange Bank, 92 U. S. 122	214
E		v. Ocean Nat. Bank, 60 N. Y. 278	489
Earp's Appeal, 28 Pa. St. 368	574	v. Smith; 65 Ill. 44	108
East Birmingham Land Co. v. Dennis, 85 Ala. 565	761	v. Trebein Co., 59 Ohio St. 316	28
Eastern Tube Co. v. Harrison, 140 Fed. 519	939	Fisher v. Essex Bank, 5 Gray (Mass.) 373	757
Eason v. Buckeye Brewing Co., 51 Fed. 156	218, 227	Fiashill Savings Institution v. National Bank, 80 N. Y. 162	353
Eaton v. Robinson, 19 R. I. 146	701	Fitzgerald v. Fitzgerald & Co. Const. Co., 44 Neb. 463	501
v. Walker, 76 Mich. 579	175	Fitzgerald & Co. Const. Co. v. Fitzgerald, 137 U. S. 98	454
Edgeworth v. Wood, 58 N. J. L. 463	90	Fleckner v. Bank, 8 Wheat. (U. S.) 351	218
Edmunds v. Illinois Central R. Co., 36 Nat. Corp. 50	52	Flinn, Assignee, v. Bagley, 7 Fed. 785	850
Edwards v. Bay State Gas Co., 91 Fed. 942	673	Florence Land & C. R. Co., In re, L. R. 29 Ch. Div. 421	360
v. Fairbanks, 27 La. Ann. 449	243	Flostroy v. Corby Coal Co., 85 Atl. (N. J.) 578	757
Eidman v. Bowman, 58 Ill. 444	428	Flynn v. Brooklyn City R. Co., 158 N. Y. 493	672
Electric Welding Co. v. Prince, 195 Mass. 242	939	Force v. Age-Herald Co., 136 Ala. 271	801
Eliot v. Freeman, 220 U. S. 178	105	Ford v. Chicago Milk Shippers' Assn., 155 Ill. 166	59
Elizabeth City Academy v. Lindsey, 6 Ired. Law (28 N. C.) 476	182	v. East Hampton Rubber Thread Co., 158 Mass. 84	570
Ellis v. Ward, 137 Ill. 509	454	Forrester v. Boston & Co. Mining Co., 21 Mont. 544	676
Elyea v. Lehigh Salt Mining Co., 169 N. Y. 29	227, 763	Forrest v. Manchester & Co. R. Co., 4 De G. & F. & J. 125	688
Empress Eng. Co., In re, L. R. 16 Ch. Div. 125	932, 936	Fortunato v. Patten, 147 N. Y. 277	757
England v. Dearborn, 141 Mass. 590	11	Foster & Sons, Limited v. Commissioners of Inland Revenue, L. R. 1 Q. B. 516	7, 109
Engliah & Co. Produce Co., In re, 2 Ch. Div. 435	932	Foster v. Seymour, 23 Fed. 65	927
Eric & Co. R. Co. v. Casey, 26 Pa. St. 287	956	Fougeray v. Cord, 50 N. J. Eq. 185	578
Eric City Iron Works v. Barber, 106 Pa. St. 125	14	Fourth Nat. Bk. of New York v. Franklyn, 120 U. S. 747	864
Erlanger v. New Sombbrero Phosphate Co., L. R. 3 App. Cas. 1218	926, 926	Fox v. Horah, 36 N. Car. (1 Ired. Eq.) 358	964
Ernest v. Nicholls, 6 H. L. Cas. 401	501	Franklin Co. v. Lewiston Savings Bank, 68 Maine 43	218, 231
Ersfeld v. Exner, 128 App. Div. (N. Y.) 135	633	Franklin Union No. 4 v. People, 220 Ill. 355	22
Ervin v. Oregon R. & Nav. Co., 27 Fed. 625	707, 726	Fred Macey Co. v. Macey, 143 Mich. 138	920
Esgen v. Smith, 113 Iowa 25	858	Freeman v. Sea View Hotel Co., 57 N. J. Eq. 68	233
European Society Arbitration Acts, In re, L. R. 8 Ch. Div. 679	245	French Bank Case, In re, 53 Cal. 495	953
Evangelical & Co. Missionary Society v. City of Boston, 204 Mass. 28	264	French v. Donohue, 29 Minn. 111	224
Evansville Public Hall Co. v. Bank of Commerce, 144 Ind. 34	501	Fritts v. Palmer, 132 U. S. 282	239
Excelsior Grain Binder Co. v. Stayner, 25 Hun (N. Y.) 91	384	Frost v. Walker, 60 Maine 468	93
Exchange Bank of Macon v. Macon Const. Co., 97 Ga. 1	10	Fulgum v. Macon & Co. R. Co., 44 Ga. 597	359
F		Fryer v. Wiedemann, 148 Ky. 379	505
Falconer v. Campbell, 2 McLean (U. S.) 195	119	G	
Farmers' Loan & Trust Co. v. N. Y. & N. R. Co., 150 N. Y. 410	726	Ganey v. Gilson, Receiver, 149 Ind. 58	827
Faulds v. Yates, 57 Ill. 416	530	Galena & Co. R. Co. v. Ennor, 116 Ill. 55	405
Fechter v. Palm Bros., 133 Fed. 462	222	Gallagher v. Asphalt Co., 65 N. J. Eq. 258	789
Ffooks v. South-Western R. Co., 1 Sm. & Giff. 142	676	v. Germania Brewing Co., 53 Minn. 214	3, 109
Fidelity Trust Co. v. Louisville Gas Co., 118 Ky. 588	231, 232	Galveston & Co. R. Co. v. Gonzales, 151 U. S. 496	85
Fild v. Lamson & Co. Mfg. Co., 162 Mass. 388	619	Gamble v. Queens County Water Co., 123 N. Y. 91	710
Fifth Avenue Bank v. Forty-second street & G St. Ferry R. Co., 137 N. Y. 231	744	Gardner v. Butler, 30 N. J. Eq. (E. & A.) 702	499

[References are to Pages.]

Gardner v. Minneapolis &c. R. Co., 73 Minn. 517	175	Greenfield Savings Bank v. Abercrombie, 211 Mass. 252	472
Garnett v. Richardson, 35 Ark. 144	167	Greenville &c. Warehouse Co. v. Planters' &c. Warehouse Co., 70 Miss. 669	300, 337
Garrett v. Kansas City Coal Min. Co., 113 Mo. 330	627	Greenwood v. Leather Shod Wheel Co., L. R. (1900) 1 Ch. Div. 421	921
Garrison Canning Co. v. Stanley, 133 Iowa 57	232	Gregg v. Sanford, 65 Fed. 151	94
Gartside Coal Co. v. Maxwell, 22 Fed. 197	171	Gregory v. Patchett, 33 Beav. 595	647
Gause v. Commonwealth Trust Co., 196 N. Y. 134	230, 322	Gress v. Knight, 135 Ga. 60	421
Geddes v. Anaconda Copper Mining Co., 197 Fed. 860	726	Griffing v. Griffing Iron Co., 61 N. J. Eq. 269	578
Gelders v. State, 164 Ala. 592	168	Gruber v. Washington &c. R. Co., N. Car. 1	353
General Electric Co. v. Wightman, 3 App. Div. (N. Y.) 118	384	Guckert v. Hackle, 159 Pa. St. 303	167
Gent v. Mfgs. &c. Ins. Co., 107 Ill. 652	929	Gunn v. Central Railroad, 74 Ga. 509	347
Geo. L. Oliver, Estate of, 136 Pa. St. 43	557	Guthrie v. Harkness, 199 U. S. 148	594
George T. Stagg Co. v. E. H. Taylor, Jr. & Sons, 113 Ky. 709	10	H	
German Sav. Bank v. Wulfekuhler, 19 Kans. 60	214	Haas Co., In re, 131 Fed. 232	557
Gibbons v. Anderson, 80 Fed. 345	491	Haas v. Universal &c. Record Co., 132 N. Y. S. 767	495
Gibbs v. Long Island Bank, 83 Hun (N. Y.) 92	549	Hackett v. Multnomah R. Co., 12 Ore. 124	224
Gilbert v. Finch, 173 N. Y. 455	472	Hageman v. Southern Electric R. Co., 202 Mo. 249	793
Gilkinson v. Third Ave. R. Co., 47 App. Div. (N. Y.) 472	738	Hagerstown &c. Improvement Co. v. Keedy, 91 Md. 430	327
Gillespie v. Fort Wayne R. Co., 17 Ind. 243	115	Hale v. Henkel, 201 U. S. 43	86
Gillette v. Chicago Title & Trust Co., 230 Ill. 373	858	Hall v. Vermont &c. R. Co., 28 Vt. 401	929
Gillett v. Missouri &c. R. Co., 55 Mo. 315	347	Hall v. Wagner, 111 App. Div. (N. Y.) 70	770
Gillis v. Bailey, 21 N. H. 149	451	Hamlin v. Toledo &c. R. Co., 78 Fed. 664	619
Glenn v. Porter, 73 Fed. 275	752	Hamor v. Taylor-Rice Engineering Co., 84 Fed. 392	212
Glover v. Lee, 140 Ill. 102	232	Hamsher v. Hamsher, 132 Ill. 273	236
Goetz v. Knie, 103 Wis. 366	428	Hanson v. Little Sisters of the Poor, 79 Md. 434	254
Gold Bluff &c. Corporation v. Whitlock, 75 Conn. 669	450	Hapgoods v. Lusch, 123 App. Div. (N. Y.) 23	384
Goodnow v. American Writing Paper Co., 72 N. J. Eq. 692	639	Harding v. American Glucose Co., 182 Ill. 551	59, 227
Goodwin v. Boston & M. R. R., 127 Fed. 986	146	Harper v. Union Mfg. Co., 100 Ill. 225	789
v. Wilbur, 104 Ill. App. 45	920	Harriman v. Northern Securities Co., 197 U. S. 244	331
Goss v. Goss, 147 App. Div. (N. Y.) 698	494	v. Southam, 16 Ind. 190	115
Gottfried v. Miller, 104 U. S. 521	230	Harris v. Mississippi Valley &c. R. Co., 51 Miss. 602	944
Goulburn Valley Butter Fact. Co. v. Bank of New South Wales, 26 Vict. L. R. 351	11	Harrison v. Thomas, 112 Fed. 22	665
Gould v. Head, 41 Fed. 240	729	Hart v. Frontino &c. Gold Min. Co., L. R. 5 Ex. 115	778, 779
v. Little Rock &c. R. Co., 52 Fed. 680	232	Harts v. Brown, 77 Ill. 226	505
Gow v. Collins &c. Lumber Co., 109 Mich. 45	172	Harvey v. Linville Improvement Co., 118 N. Car. 693	539
Grafflin Co. v. Woodside, 87 Md. 146	548	Haskell v. Worthington, 94 Mo. 56	413
Granby Min. Co. v. Richards, 95 Mo. 106	119	Haslam v. First Nat. Bank, 79 Minn. 1	757
Grand River Bridge Co. v. Rollins, 13 Colo. 4	932	Hastings Lumber Co. v. Edwards, 188 Mass. 587	428
Granger's Life & Health Ins. Co. v. Kamper, 73 Ala. 325	621	Havemeyer v. Superior Court, 84 Cal. 327	956
Grant v. Attrill, 11 Fed. 469	514	Hawley v. Upton, 102 U. S. 314	360
Graves v. Brooks, 117 Mich. 424	852	Hayden v. Hayden, 241 Ill. 183	237
v. Hemenway, 98 N. E. (Mass.) 789	574	v. Official Hotel Red-Book &c. Co., 42 Fed. 875	229
Great Southern Fireproof Hotel Co. v. Jones, 177 U. S. 449	94	v. Williams, 96 Fed. 279	799
Green v. Abietine Medical Co., 96 Cal. 322	639	Hayward v. Davidson, 41 Ind. 214	237
v. Hedenberg, 159 Ill. 489	665	v. Leeson, 176 Mass. 310	920
Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 738	413	Hazard v. Wight, 201 N. Y. 399	785
		Hazlehurst v. Savannah &c. R. Co., 43 Ga. 13	602
		Heath v. Barmore, 50 N. Y. 302	956
		v. Silverthorn &c. Co., 39 Wis. 146	115
		Hendee v. Pinkerton, 14 Allen (Mass.) 381	231
		Henderson v. Bank of Australasia, 40 Ch. Div. 170	233

[References are to Pages.]

Henderson v. Mayfield Woolen Mills, 153 Ala. 625	886	I		
Hennessy v. Muhleman, 40 App. Div. (N. Y.) 175	233		Jauch v. de Socarras, 56 N. J. Eq. 524	789
Hess v. Sloane, 66 App. Div. 522	230		Illinois Steel Co. v. O'Donnell, 156 Ill. 624	232
Hibbard v. Ryan, 46 Ill. App. 313	13		Ince Hall Rolling Mills Co., In re, L. R. 23 Ch. Div. 545	625
Hibernia Ins. Co. v. St. Louis &c. Transp. Co., 13 Fed. 516	28		Indianapolis Furnace &c. Co. v. Her- kimer, 46 Ind. 142	387
Higgins v. Lansingh, 154 Ill. 301	611		Insurance Co. v. Dunscomb, 108 Tenn. 724	956
Higginson & Dean, In re, L. R. (1899) 1 Q. B. Div. 325	964		Interstate Telegraph Co. v. Baltimore & Ohio Tel. Co., 51 Fed. 49	52
Hillard v. Allegheny Geometrical Wood Carving Co., 173 Pa. St. 1	829		Isle of Wight R. Co. v. Tahourdin, L. R. 25 Ch. Div. 320	450
Hill v. Murphy, 98 N. E. (Mass.) 781	472			
v. Nisbet, 100 Ind. 341	215	J		
Hinckley v. Schwarzschild & Sulzberger Co., 107 App. Div. (N. Y.) 470	611		Jackson v. Brown, 5 Wend. (N. Y.) 590	231
Hinkley v. Sac &c. Line Co., 132 Iowa 396	929		v. Ludeling, 21 Wall. (U. S.) 616	518
Hirshfeld v. Fitzgerald, 157 N. Y. 166	864		Jacobson v. Brooklyn Lumber Co., 184 N. Y. 152	494, 672
Hobgood v. Ehlen, 141 N. Car. 344	858		James v. Railroad Co., 6 Wall. (U. S.) 752	508
Hodge v. U. S. Steel Corporation, 64 N. J. Eq. 111	689		Janney v. Minneapolis Industrial Expo- sition, 79 Minn. 488	505
Hoffman v. Reichert, 147 Ill. 274	509		Jennie Clarkson Home v. Missouri K. & T. R. Co., 182 N. Y. 47	770
Holmes &c. Mfg. Co. v. Holmes &c. Metal Co., 127 N. Y. 252	218, 227, 231		Jemison v. Citizens' Savings Bank, 122 N. Y. 135	322
Holmes v. Willard, 125 N. Y. 75	231		J. G. Brill Co. v. Norton &c. R. Co., 189 Mass. 431	233
Home Fire Ins. Co. v. Barber, 67 Nebr. 644	39		Johns v. Johns, 1 Ohio St. 350	108
Hooker v. Midland Steel Co., 215 Ill. 444	514		Johnson v. Kessler, 76 Iowa 411	128
Hoole v. Great Western R. Co., L. R. 3 Ch. App. Cas. 262	698		v. Norway, (1623) Winch. 37	940
Hoolley, In re, 2 Q. B. 579	355		v. Okerstrom, 70 Minn. 303	166
Hopkins v. Roseclaire Lead Co., 72 Ill. 373	10		v. Wabash &c. Plank Road Co., 16 Ind. 389	382
Hopkin v. Buffum, 9 R. I. 513	523		Johnston v. Laffin, 103 U. S. 800	745
Horbach v. Marsh, 37 Nebr. 22	505		Jones v. Aspen Hardware Co., 21 Colo. 263	168
Hornblower v. Crandall, 7 Mo. App. 220	921		v. Habersham, 107 U. S. 174	264
Horne v. Boston & M. R. R., 18 Fed. 50	146		Jones' Estate, 172 N. Y. 575	105
Hough v. Cook County Land Co., 73 Ill. 23	327		Jones v. Guaranty &c. Co., 101 U. S. 622	231
House of Mercy v. Davidson, 90 Tex. 529	257		v. Smith, (Tex. Civ. App.)	929
Hoyle v. Plattsburgh &c. R. Co., 54 N. Y. 314	493, 505		Judah v. American Live Stock Ins. Co., 4 Ind. 333	384
Hoyt v. McCallum, 102 Ill. App. 287	166	K		
v. Thompson's Exr., 19 N. Y. 207	440, 451		Kaiser v. Lawrence Savings Bank, 56 Iowa 104	167
Hubbard v. Weare, 79 Iowa 678	554		Kaufman v. Charlottesville Woolen Mills Co., 93 Va. 673	563, 578
v. Worcester Art Museum, 179 Fed. 406	265		Kavanaugh v. Commonwealth Trust Co., 64 Misc. (N. Y.) 303	490
Hughesdale Mfg. Co. v. Vanner, 12 R. I. 491	168		v. Gould, 147 App. Div. (N. Y.) 281	490
Huguenot Mills v. Jempson, 68 S. Car. 363	224		Kean v. Johnson, 9 N. J. Eq. 401	231
Hun v. Cary, 82 N. Y. 65	490		Kellogg v. Douglas County Bank, 58 Kans. 43	28
Hunter v. Roberts, 83 Mich. 63	578		Kelner v. Baxter, L. R. 2 C. P. 174, 185	936
Humphreys v. McKissock, 140 U. S. 304	7		Kelly v. Biddle, 180 Mass. 147	224
v. Mooney, 5 Colo. 282	132		Kennebec &c. R. Co. v. Kendall, 31 Maine 470	396
Hurd v. N. Y. &c. Laundry Co., 167 N. Y. 89	785		Keokuk Elec. Ry. &c. Co. v. Weisman, 146 Iowa 679	39
Hurst v. Meason, 4 Watts (Pa.) 346	108		Kessler v. Ensley Co., 123 Fed. 546	684
Hussey v. Norfolk &c. Ry., 98 N. Car. 34	13		Kidwelly Canal Co. v. Raby, 2 Price (Eng. Excheg.) 93	382
Hutchinson v. Green, 91 Mo. 367	232, 428		Kingsbury Collieries, Ltd., In re, L. R. 2 Ch. Div. 259	231
v. Stadler, 85 App. Div. (N. Y.) 424	822		Kings County Elevated R. Co., Matter of, 105 N. Y. 97	948
v. Western &c. R. Co., 6 Heisk. (Tenn.) 634	353		Klaus, In re, 67 Wis. 401	735
v. Young, 80 App. Div. (N. Y.) 246	822			
v. Young, 93 App. Div. (N. Y.) 407	822			
Hyatt v. Allen, 56 N. Y. 553	557			
Hybart v. Parker, 4 C. B., N. S. 209	93			

[References are to Pages.]

Klein v. Independent Brewing Assn., 231 Ill. 594	509	London India Rubber Co., In re, L. R. 5 Eq. 518, 519	557, 619
Knowlton v. Congress &c. Spring Co., 57 N. Y. 518	622	Lord v. Equitable Life Assur. Society, 47 Misc. (N. Y.) 187	121
Knox v. Childersburg Land Co., 86 Ala. 370, 180	413	v. Equitable Life Assur. Society, 194 N. Y. 212	521
v. Eden Musee American Co., 148 N. Y. 441	769	v. Yonkers Fuel Gas Co., 99 N. Y. 547	231
Kodak, Ld. v. Clark, 2 K. B. 450	46	Long Island W. S. Co. v. Brooklyn, 166 U. S. 685	122
Koehler v. Black River &c. Iron Co., 2 Black (U. S.) 715	509	Louisville &c. R. Co. v. Louisville Trust Co., 174 U. S. 552	232
Kraft v. Griffon Co., 82 App. Div. (N. Y.) 29	842	Louisville Banking Co. v. Eisenman, 94 Ky. 83	10
v. West Side Brewery Co., 219 Ill. 205	231	Louisville, Cincinnati and Charleston R. Co. v. Letson, 2 How. (U. S.) 497	81
L		Loverin v. McLaughlin, 161 Ill. 417	167
Lake Ontario &c. R. Co. v. Mason, 16 N. Y. 451	382	Low v. Connecticut &c. R. R., 45 N. H. 370	932
Lake Superior Iron Co. v. Drexel, 90 N. Y. 87	853	Lowe v. Ring, 123 Wis. 370	454
Lamming v. Galusha, 81 Hun (N. Y.) 247	182	Lowne v. Amer. Fire Ins. Co., 6 Paige Ch. (N. Y.) 482	566
Lancaster v. Amsterdam Improvement Co., 140 N. Y. 576	233	Lubbock v. British Bank of South America, 2 Ch. Div. 198	557
Lane v. Albertson, 78 App. Div. (N. Y.) 607	105	Lucas v. Friant, 111 Mich. 426	505
Lange v. Burk, 69 Ark. 85	46	v. White Line Transfer Co., 70 Iowa 541	232
Lang v. Lutz, 180 N. Y. 254	864	Lund v. Wheaton Roller Mill Co., 50 Minn. 36	757
Lantrey v. Wallace, 182 U. S. 536	829	Luak v. Riggs, 65 Nebr. 258	28
Larimer v. Beardale, 130 Iowa 706	738	Lyell Ave. Lumber Co. v. Lighthouse, 137 App. Div. (N. Y.) 422	168
Laurel Springs Land Co. v. Fougerey, 50 N. J. Eq. 756	578	Lyndeborough Glass Co. v. Mass. Glass Co., 111 Mass. 315	233
Lawford v. Billerica &c. Council, L. R. 1 K. B. 772	230	Lyons-Thomas Hardware Co. v. Perry Stove Mfg. Co., 86 Tex. 143	794
Lawrence v. Nelson, 21 N. Y. 158	785	M	
Leazure v. Hillegas, 7 S. & R. (Pa.) 313	239	McAfee v. Zettler, 103 Ga. 579	673
LeBlanc, Matter of, 14 Hun (N. Y.) 8	566	McAllen v. Woodcock, 60 Mo. 174	505
Leeds &c. Investment Co. v. Shepherd, L. R. 36 Ch. Div. 787	477	McCartee v. Orphan Asylum Society, 9 Cow. (N. Y.) 437	265
Lehigh Bridge Co. v. Lehigh Coal & Navigation Co., 4 Rawle (19 Pa.) 9	944	McArthur v. Times Printing Co., 48 Minn. 319	936
Leigh v. American Brake Beam Co., 205 Ill. 147	232	McAuley v. Columbus &c. R. Co., 83 Ill. 348	184
Leighton v. Leighton Lee Assn., 146 App. Div. (N. Y.) 255	864	McCabe v. Goodfellow, 133 N. Y. 89	105
Leinkauf v. Calman, 110 N. Y. 50	230	McC Campbell v. Fountain Head R. Co., 111 Tenn. 55	676
LeRoy v. Globe Ins. Co., 2 Edw. Ch. (N. Y.) 657	566	McCarthy v. Lavasche, 89 Ill. 270	175
Leslie v. Lorillard, 110 N. Y. 519	233	McCarthy Portable Elevator Co., In re, 196 Fed. 247	499
Leurey v. Bank of Baton Rouge, 131 La. —	779	McClaine v. Rankin, 197 U. S. 154	864
Levin v. Chicago &c. Coke Co., 64 Ill. App. 393	683	McClure v. Law, 161 N. Y. 78	509
Lexington &c. Ins. Co. v. Page, 17 B. Mon. (Ky.) 412	440	McComb v. Barcelona Apartment Assn., 134 N. Y. 598	501
Leyner Engineering Works v. Kepner, 163 Fed. 605	873	McCoy v. World's Columbian Exposi- tion, 186 Ill. 356	387
Leyson v. Davis, 7 Mont. 220	738	McCullough v. Moss, 5 Denio (N. Y.) 567	440
Lincoln Shoe Mfg. Co. v. Sheldon, 44 Nebr. 279	391	McCutcheon v. Merz Capsule Co., 71 Fed. 787	332
Lipscomb's Adm'r v. Condon, 56 W. Va. 416	757	McElroy v. Minnesota &c. Horse Co., 96 Wis. 317	314
Liquidators of Imperial Mercantile Credit Assn. v. Coleman, L. R. 6 Eng. Ir. App. Cas. 189	509	McGinty v. Athol Reservoir Co., 155 Mass. 183	944
Liverpool Household Stores Associa- tion, In re, 62 L. T. R. 873	471	McGraw, Matter of, 111 N. Y. 66	254
Loewenthal v. Rubber Reclaiming Co., 52 N. J. Eq. 440	440	McIntyre v. Ajax Min. Co., 28 Utah 162	508
London County Council v. Attorney- General, App. Cas. 165	205	McKee v. Home &c. Trust Co., 122 Iowa 731	531
London Financial Assn. v. Kelk, 26 Ch. Div. 107	205, 464	McKinley v. Wheeler, 130 U. S. 630	59
		McLaran v. Crescent Planing Mill Co., 117 Mo. App. 40	566, 567, 570
		McLean v. Wright Medicine Co., 96 Mich. 479	745
		McLennan v. Hopkins, 2 Kan. App. 260	168

[References are to Pages.]

McLoath v. Hunt, 154 N. Y. 179	574	Merchants' & Planters' Line v. Wagoner, 71 Ala. 581	944
McMahon v. Raube, 47 N. Y. 67	105	Merchants' Bank v. Livingston, 74 N. Y. 223	763
McMillan v. Maysville & C. R. Co., 15 R. Mon. (Ky.) 218	408	v. Weill, 163 N. Y. 486	763
McMurry v. Montgomery & Temple Co., 86 Ky. 206	505	Merrick v. Peru Coal Co., 61 Ill. 472	505
McNab v. McNab & Mfg. Co., 62 Hun (N. Y.) 18	494, 578	Metropolitan Elevated R. Co. v. Manhattan Elevated R. Co., 11 Daly (N. Y.) 373	428, 493, 501, 505
McNaught v. Fisher, 96 Fed. 168	370	Metropolitan Stock Exchange v. Lyndonville Nat. Bank, 76 Vt. 303	300
McNulta v. Corn Belt Bank, 164 Ill. 427	397, 735	Meyer v. Blair, 109 N. Y. 600	406
McVity v. Albro Co., 90 App. Div. (N. Y.) 109	554	Mig's Commercial Co. v. Heckscher, 144 App. Div. (N. Y.) 600	864
MacDougall v. Gardiner, L. R. 1 Ch. Div. 13	647	Middlecott Hotel Co. v. Yeomans, 89 Ill. App. 170	413
MacGregor v. Official Manager of Deal & C. R. Co., 22 Law J. (N. S.) Q. B. 69	277	Miller v. Brodish, 69 Iowa 278	557
Machinists' Nat. Bank v. Field, 126 Mass. 345	744	v. Coal Co., 31 W. Va. 836	175, 182
Magerstadt v. Schaefer, 213 Ill. 351	757	v. Insurance Co., 92 Tenn. 167	314
Magee v. Pacific Improvement Co., 98 Cal. 678	313	Miller & Lux v. East Side Canal & Co., 211 U. S. 293	33
Malone v. Lancaster Gas & C. Co., 182 Pa. St. 309	209	Miller v. Murray, 17 Colo. 408	523
Man v. Boykin, 79 S. Car. 1	749	v. Wildcat Gravel Road Co., 52 Ind. 51	360
Manhattan Brass Co. v. Webster & Queensware Co., 37 Mo. App. 145	444	Mills, In re, 125 App. Div. (N. Y.) 730	763
Manufacturers' & C. Bldg. Co. v. Landay, 219 Ill. 168	232, 541	Mills, Matter of, 125 App. Div. (N. Y.) 730	770
Mapleton Bank v. Standrod, 8 Idaho 740	757	Miner v. Belle Isle Ice Co., 93 Mich. 97	494, 953
Marble Co. v. Harvey, 92 Tenn. 115	300	Minneapolis Harvester Works v. Libby, 24 Minn. 327	368
Marchand v. Loan & Pledge Assn., 26 La. Ann. 389	929	Minneapolis v. Minneapolis & C. R. Co., 215 U. S. 417	231
Marion Trust Co. v. Blish, 170 Ind. 686	827	Minneapolis Threshing Machine Co. v. Davis, 40 Minn. 110	405
Marr v. Marr, 72 N. J. Eq. 797	505	Minot v. Paine, 99 Mass. 101	574
Marshall v. Baltimore & C. R. Co., 16 How. (U. S.) 314	81	Mississippi & C. R. Co. v. Gaster, 20 Ark. 455	363
v. Farmers' & C. Bank, 85 Va. 676	491	Mobile & C. R. Co. v. Tennessee, 153 U. S. 486	557
Marsh v. Kaye, 168 N. Y. 196	881	Mobile Land Improvement Co. v. Gass, 142 Ala. 520	499
Marson v. Deither, 49 Minn. 423	360	Moffatt v. Farquhar, L. R. 7 Ch. Div. 591	729
Martin v. Niagara Falls Paper Mfg. Co., 122 N. Y. 165	233	Mohawk Nat. Bank v. Schenectady Bank, 78 Hun (N. Y.) 90	549, 735
Marvin v. Anderson, 111 Wis. 387	793	Mokelumne & Mining Co. v. Woodbury, 14 Cal. 424	132
Mason v. Carrothers, 105 Maine 392	924, 926	Monongahela Bridge Co. v. Pittsburg & C. Tract Co., 196 Pa. St. 25	11
Matthews v. Hoagland, 48 N. J. Eq. 455	738	Montana Tonopah Min. Co. v. Dunlap, 196 Fed. 612	454
Mayor & C. of Norwich v. Norfolk R. Co., 4 Ellis & Bl. 397	277	Monteruma Cattle Co. v. Dake, 16 Colo. App. 139	696
Mechanics' & Machine Co. v. Hall, 121 Mass. 272	396	Montgomery Light Co. v. Lahey, 121 Ala. 131	684
Melbado v. Port Alegre, N. H. & B. R. Co., L. R. 9 C. P. 505	936	Montgomery v. Phillips, 53 N. J. Eq. 203	812
Melvin v. Lamar Ins. Co., 80 Ill. 446	405, 785	Monument Nat. Bank v. Globe Works, 101 Mass. 57	233
Memford v. Ecuador Development Co., 111 Fed. 639	726	Moore & C. Hardware Co. v. Towers Hardware Co., 87 Ala. 206	3
Memphis & Charleston R. R. Co. v. Grayson, 88 Ala. 572	684	Moore v. Moore Mica Paint Co., 135 N. Y. S. 210	440
Memphis & Little Rock R. Co. v. Dow, 120 U. S. 287	639	Moore v. Silver Valley Min. Co., 104 N. Car. 534	684
Memphis & Railroad Co. v. Railroad Commissioners, 112 U. S. 609	78	v. Whitcomb, 48 Mo. 543	946
v. Sullivan, 57 Ga. 240	391, 397, 420	Morey v. Fish Bros. Wagon Co., 108 Wis. 520	578
v. Wood, 88 Ala. 630	521	Morgan v. Lewis, 46 Ohio St. 1	214
Memphis Barrel & C. Co. v. Ward, 99 Tenn. 172	794	v. Skiddy, 62 N. Y. 319	920
Mercantile Bank v. Tennessee, 161 U. S. 161	78	v. Struthers, 131 U. S. 246	406
Mercantile Library Hall Co. v. Pittsburg Library Assn., 173 Pa. St. 30	428	Mormon Church v. United States, 136 U. S. 1	956
Mercantile Statement Co. v. Kneal, 51 Minn. 263	421	Morris v. Hall, 41 Ala. 510	243
Merchants & C. Improvement Co. v. Chicago & C. Bldg. Co., 106 Ill. App. 17	233		

[References are to Pages.]

Morrison v. Indianapolis &c. R. Co., 166 Ind. 511	184	Nicoll v. New York &c. R. Co., 12 N. Y. 121	231
Morton v. Hamilton College, 100 Ky. 281	932	Niles v. N. Y. Central &c. R. Co., 176 N. Y. 119	672
Moses v. Soule, 63 Misc. (N. Y.) 203	211	Norris v. Staps, Hobart's 210b, 211a	252
Mott v. Danville Seminary, 129 Ill. 403	956	North American Land & Timber Co. v. Watkins, 109 Fed. 101	710
Moxham v. Grant, 69 L. J. Q. B. 97	457	Northern Securities Co. v. United States, 193 U. S. 197	66
Mozley v. Alston, 1 Ph. 790	647	North Hudson &c. Loan Assn. v. Childs, 82 Wis. 460	490
Mt. Sterling &c. Road Co. v. Little, 14 (Bush) Ky. 429	356	North Shore &c. Ferry Co., Matter of, 63 Barb. (N. Y.) 556	523
Muncie Pulp Co., In re, 139 Fed. 546	52	Northwestern Union Packet Co. v. Shaw, 37 Wis. 655	331
Muncy Traction Engine Co. v. De La Green, 143 Pa. St. 269	370	Norton v. Derry Nat. Bank, 61 N. H. 589	300
Munson v. Syracuse &c. R. Co., 103 N. Y. 58	494	N. Y. Airbrake Co. v. International Steam Pump Co., 64 Misc. (N. Y.) 347	46
Mutter v. Eastern &c. R. Co., L. R. 38 Ch. Div. 92	597	N. Y. & Oswego M. R. R. Co. v. Van Horn, 57 N. Y. 473	384
Myers v. Sturgis, 123 App. Div. (N. Y.) 470	391	N. Y. &c. R. Co. v. Schuyler, 34 N. Y. 30	622
N		v. Ketchum, 27 Conn. 170	929
Nanney v. Morgan, L. R. 37 Ch. Div. 346	736	N. Y. & R. v. Nickals, 119 U. S. 296	578
Nantasket Beach Steamboat Co. v. Shea, 182 Mass. 147	239	N. Y. &c. Bridge Co. v. Smith, 148 N. Y. 540	948
Nappanee Canning Co. v. Reid, 159 Ind. 614	232	N. Y. Elevated R. Co., Matter of, 70 N. Y. 327	948
Nashua &c. R. Corp. v. Boston &c. R. Corp., 136 U. S. 356	137	O	
National &c. Beam Co. v. Chicago &c. Equipment Co., 226 Ill. 28	501	Oakes v. Cattaraugus Water Co., 143 N. Y. 430	936
National Bank v. Case, 99 U. S. 628	246	O' Bear Jewelry Co. v. Volfer, 106 Ala. 205	785
v. Graham, 100 U. S. 699	353	Occum Co. v. Sprague Mfg. Co., 34 Conn. 529	239
v. Matthews, 98 U. S. 621	239	O'Conner &c. Mfg. Co. v. Coosa Furnace Co., 95 Ala. 614	501
v. Texas Investment Co., 74 Tex. 421	128	O'Connor Mining & Mfg. Co. v. Coosa Furnace Co., 95 Ala. 614	800
v. Watsontown Bank, 105 U. S. 217	735	O'Connor v. Virginia &c. Power Co., 48 Misc. (N. Y.) 228	665
v. Young, 14 Stew. Eq. (N. J.) 531	231	Oelbermann v. N. Y. &c. R. Co., 76 Hun (N. Y.) 613	521
National Bank of Auburn v. Dillingham, 147 N. Y. 603	822	Ohio &c. R. Co. v. Wheeler, 1 Black (U. S.) 286	137
National Funds Assur. Co., In re, L. R. 10 Ch. Div. 118	472	Oil Creek &c. R. Co. v. Pennsylvania Transportation Co., 83 Pa. St. 160	313
Natal Land &c. Co. v. Pauline &c. Syndicate, (1904) A. C. 120	936	Old Dominion Copper &c. Smelting Co. v. Bigelow, 203 Mass. 159	11
National Loan and Investment Co. v. Rockland Co., 94 Fed. 335	454	v. Bigelow, 188 Mass. 315	926
National Park Bank v. German-American &c. Security Co., 116 N. Y. 281	231, 233	Old Dominion Copper Mining Co. v. Lewisohn, 136 Fed. 915	927
National Society v. American Surety Co., 56 Misc. (N. Y.) 627	182	Oldtown &c. R. Co. v. Veazie, 39 Maine 571	420
National Tube Works Co. v. Gilfillan, 124 N. Y. 302	858	Oler v. Baltimore & Randallstown Railroad, 41 Md. 583	384
New Albany v. Burke, 11 Wall. (U. S.) 96	397, 785	Oliver v. Bank of England, 1 Ch. Div. 610	779
New Castle &c. R. Co. v. Simpson, 21 Fed. 533	331, 639	v. Oliver, 118 Ga. 362	518
Newcomb v. Reed, 12 Allen (Mass.) 362	132	Olympia, Ltd., In re, L. R. (1892) 2 Ch. Div. 153	913
New Hamp. Central R. Co. v. Johnson, 30 N. H. 390	396	Olympia Min. Co. v. Kerns, 13 Idaho 514	413
New Memphis Gas Light Co. Cases, 105 Tenn. 268	505	Omaha Hotel Co. v. Wade, 7 Otto (U. S.) 13	59
New Monshonaland Exploration Co., In re, 3 Ch. Div. 577	472	O'Neill v. Ternes, 32 Wash. 528	514
Newton Mfg. Co. v. White, 42 Ga. 148	10	Ontario Salt Co. v. Merchants' Salt Co., 18 Grant's Ontario Ch. 540	222
Newton Nat. Bank v. Newbegin, 74 Fed. 135	421	Ooregum Gold Mining Co. v. Roper, A. C. (1892) 125	625, 852
New York &c. Ins. Co. v. Ely, 5 Conn. 560	300	Oregon Short Line R. Co. v. Postal Tel. Cable Co., 111 Fed. 842	184
New York &c. R. Co. v. Haring, 47 N. J. L. 137	353	Ottawa &c. R. Co. v. Black, 79 Ill. 262	416
New York Cable Co. v. Mayor &c. of New York, 104 N. Y. 1	184		
Nicholson v. Franklin Brewing Co., 82 Ohio St. 94	549		

TABLE OF CASES CITED.

xxiii

[References are to Pages.]

Ottumwa Screen Co. v. Stodghill, 103 Iowa 437	757	People's Bank v. Gridley, 91 Ill. 457	757
Overend & Gurney Co. v. Gibb, L. R. 5 H. L. 480	477	People's Home Savings Bank v. Sadler, 1 Cal. App. 189	548
Owensboro Wagon Co. v. Bliss, 132 Ala. 253	166, 948	Peoria &c. R. Co. v. Thompson, 103 Ill. 187	628
P			
Pacific &c. Pickle Works v. Smith, 145 Cal. 352	494	Peoria Star Co. v. Cutright, 115 Ill. App. 492	300
Pacific Fruit Co. v. Coon, 107 Cal. 477	396	Percival v. Wright, 2 Ch. Div. 421	514
Pacific National Bank v. Eaton, 141 U. S. 227	360	Perkins v. Lyons, 111 Iowa 192	749
Palmer v. Bank of Zumbrota, 72 Minn. 266	622	v. Sanders, 56 Miss. 733	115
v. Lawrence, 3 Sandf. Super. Ct. (N. Y.) 161	128	Perrine v. Levin, 68 Misc. (N. Y.) 327	168
v. Ring, 113 App. Div. (N. Y.) 643	11	Perry v. Pearson, 135 Ill. 218	514
Parish v. Wheeler, 22 N. Y. 494	243	Peru Plow and Implement Co. v. Har-ker, 144 Fed. 673	243
Parker v. Bethel Hotel Co., 96 Tenn. 252	11, 945, 948	Philadelphia &c. R. Co. v. Conway, 177 Pa. St. 364	406
v. Nickerson, 112 Mass. 195	509	Philips v. Wickham, 1 Paige Ch. (N. Y.) 590	944
Parsons v. Joseph, 92 Ala. 403	676	Phoenix Life Assurance Co., In re, 2 Johns. & Hemm. 441	314
Patent File Co., In re, L. R. 6 Ch. App. Cas. 83	231	Phoenix Warehousing Co. v. Badger, 67 N. Y. 294	384, 416
Patterson v. Lynde, 112 Ill. 196	785	Pierce v. Commonwealth, 104 Pa. St. 150	523
Paul v. Virginia, 8 Wall. (U. S.) 168	85	Pietsch v. Krause, 116 Wis. 344	628
Paxon v. Sweet, 1 Green 196	544	v. Milbrath, 123 Wis. 647	926
Pearce v. Madison &c. R. Co., 21 How. (U. S.) 441	233	Pinkerton v. Pennsylvania Traction Co., 193 Pa. St. 229	182
Pearson v. Concord R., 62 N. H. 537	218	Piper v. Rhodes, 30 Ind. 309	132
Peat v. Clayton, 1 Ch. Div. 659	744	Pittsburgh &c. R. Co. v. Biggar, 34 Pa. St. 455	402
Peck v. Noce, 154 Cal. 351	869	v. Stewart, 41 Pa. St. 54	398
Pelton v. Spider &c. Lumber Co., 117 Wis. 569	233	Pittsburg Min. Co. v. Spooner, 74 Wis. 307	907
Pender v. Lushington, L. R. 6 Ch. Div. 70	707	Plank's Tavern Co. v. Burkhard, 87 Mich. 182	370
Pennell v. Lothrop, 191 Mass. 357	936	Planters' & Miners' Bank v. Padgett, 69 Ga. 159	175
Pennington v. Gittings, 2 Gill & J. (Md.) 208	738	Planters' &c. Packet Co. v. Webb, 144 Ala. 666	384, 387, 396
Pennsylvania R. Co.'s Appeal, In re, 86 Pa. St. 80	763	Planters' Bank of Farmville v. Whit-tle, 78 Va. 737	815
People v. Amer. Press Assn., 148 App. Div. (N. Y.) 651	597	Plaskynaston Tube Co., In re, L. R. 23 Ch. Div. 542	625
v. Ascasora, 1 Hill (N. Y.) 616	90	Pollitz v. Wabash R. Co., 150 App. Div. (N. Y.) 715	639, 673
v. Ballard, 134 N. Y. 269	227	Pond v. Framingham &c. R. Co., 130 Mass. 194	801
v. Cal. Safe Deposit & Tr. Co., 126 Pac. (Cal.) 516	829	Porter v. Plymouth Gold Mining Co., 29 Mont. 347	211
v. Campbell, 144 N. Y. 166	209	v. Rockford &c. R. Co., 76 Ill. 561	113
v. Carter, 122 Mich. 668	193	Postal Tel. Cable Co. v. Oregon Short Line R. Co., 114 Fed. 787	184
v. Chicago Gas Trust Co., 130 Ill. 268	218	Poughkeepsie &c. Plankroad Co. v. Griffin, 24 N. Y. 150	384
v. Coleman, 133 N. Y. 279	105	Poulton v. London &c. R. Co., L. R. 2 Q. B. Cas. 534	347
v. Crossley, 69 Ill. 195	531	Powell v. Murray, 3 App. Div. (N. Y.) 273	233
v. Dashaway Assn., 84 Cal. 114	951	Prescott Nat. Bank v. Butler, 157 Mass. 548	313
v. Kankakee River Improvement Co., 103 Ill. 491	950	Preston v. Loughran, 58 Hun (N. Y.) 210	505
v. Koenig, 133 App. Div. (N. Y.) 756	611	Price v. Holcomb, 89 Iowa 123	229
v. Montecito Water Co., 97 Cal. 276	133	v. Price's Heirs, 6 Dana (Ky.) 107	108
v. Morgan, 178 N. Y. 433	113	Proprietors v. Dickinson, 6 Gray (72 Mass.) 586	416
v. Moss, 187 N. Y. 410	233	Protection Life Ins. Co. v. Osgood, 93 Ill. 69	745
v. New York &c. R. Co., 129 N. Y. 474	136	Puget Sound Nat. Bank v. Fisher, 52 Wash. 246	239
v. North River Refining Co., 121 N. Y. 582	59, 222, 951	Pullman Palace Car Co. v. Missouri &c. R. Co., 115 U. S. 587	52
v. Pullman's Palace Car Co., 175 Ill. 125	205	Q	
v. Rochester &c. Light Co., 195 N. Y. 102	22	Quartz Gold Mining Co., In re, 157 Fed. 243	428
v. Rose, 219 Ill. 46	92		
v. Rosenstein-Cohn Cigar Co., 131 Cal. 153	948		
v. Selfridge, 52 Cal. 331	133		
v. St. Louis &c. R. Co., 176 Ill. 512	619		
v. Woodbury Dermatological Inst., 192 N. Y. 454	22, 233		

[References are to Pages.]

Queen v. Arnand, 9 Q. B. (Adol. & El.) 806	7	Runner, Assignee, v. Dwiggins, 147 Ind. 238	850
Queen v. Great North. Ry. Co., 9 Q. B. 316	22	Russell v. American Gas & Elec. Co., 136 N. Y. S. 602	699
Quick v. Lemon, 105 Ill. 578	355	v. Rock Run Fuel Gas Co., 184 Pa. St. 102	717
Quincy v. Chicago &c. R. Co., 94 Ill. 537	231	v. Temple, 3 Dane's Abr. (Mass.) 108	108
R			
Rafferty v. Donnelly, 197 Pa. St. 423	514, 701	Rutherford v. Hill, 22 Ore. 218	167
Rainford v. James Keith & Blackman Co., Ltd., L. R. (1905) 1 Ch. Div. 296	744	Rutland &c. R. Co. v. Thrall, 35 Vt. 536	420, 602
Ramsey v. Thompson Mfg. Co., 116 Mo. 313	829	Rutter v. Chapman, 8 M. & W. 1	115
Rankin v. Cooper, 149 Fed. 1010	491	Ryan v. Grisinger, 136 N. Y. S. 134	509
v. Emigh, 218 U. S. 27	325	S	
Rathbone v. Ayre, 121 App. Div. (N. Y.) 355	852	Sage v. Culver, 147 N. Y. 241	672
Rector v. Hartford Deposit Co., 190 Ill. 380	237	St. Joseph &c. R. Co. v. Shambaugh, 106 Mo. 557	115, 184
Redhead v. Parkway Driving Club, 148 N. Y. 471	509	St. Louis &c. Railroad Co. v. Dalby, 19 Ill. 352	14
Red Wing Hotel Co. v. Friedrich, 26 Minn. 112	408	v. Indianapolis &c. R. Co., 9 Bist. (U. S.) 144	146
Reed v. Boston Machine Co., 141 Mass. 454	622	v. James, 161 U. S. 545	146
v. Home Savings Bk., 130 Mass. 443	13	St. Paul &c. R. Co. v. Robbins, 23 Minn. 439	360
v. Richmond St. Ry. Co., 50 Ind. 342	132	Salem Mill Dam Corporation v. Ropes, 6 Pick. (Mass.) 23	391
Reichwald v. Commercial Hotel Co., 106 Ill. 439	794, 945	Salomon v. Salomon & Co., L. R. App. Cas. 22	46
Remington Paper Co. v. O'Dougherty, 65 N. Y. 570	182	Saltmarsh v. Spaulding, 147 Mass. 224	505
Rhawn v. Edge Hills Furnace Co., 201 Pa. 637	11	San Diego &c. R. Co. v. Pacific Beach Co., 112 Cal. 53	501
Rhodes v. Piper, 40 Ind. 369	132	Sanford Fork & Tool Co. v. Howe, Brown & Co., Ltd., 157 U. S. 312	794, 812
R. v. Hughes, 7 B. & C. 708	115	San Joaquin Land & Water Co. v. Beecher, 101 Cal. 70	396
Rice v. Gilbert, 173 Ill. 348	757	Santa Clara County v. Southern Pac. R. Co., 118 U. S. 394	85
v. Rockefeller, 134 N. Y. 174	729	Saranac & L. P. R. Co. v. Arnold, 167 N. Y. 368	11
v. Rock Island &c. R. Co., 21 Ill. 93	387	Sargent v. Franklin Ins. Co., 8 Pick. (Mass.) 90	729
Richards v. Hollday, 92 Fed. 798	812	Savage v. Walshe, 26 Ala. 619	944
Richardson v. Vermont &c. R. Co., 44 Vt. 613	578	Schenectady &c. Plank Road Co. v. Thatcher, 1 Kern. (N. Y.) 102	128, 391, 420, 421
Richelieu Hotel Co. v. International Military Encampment Co., 140 Ill. 248	233, 370	Schwab v. Potter Co., 194 N. Y. 409	227
Rickerson Roller-Mill Co. v. Farrell Foundry & Mach. Co., 75 Fed. 554	842	Scott v. Depeyster, 1 Edw. Ch. (N. Y.) 513	464
Rider v. Fritchey, 49 Ohio St. 285	864	v. Dewcese, 181 U. S. 202	368, 829, 830
v. Union India Rubber Co., 5 Bosw. (N. Y.) 85	457	v. Eagle Fire Co., 7 Paige (N. Y.) 198	578
Ringler & Co., Matter of, 204 N. Y. 30	451	v. Latimer, 89 Fed. 843	368
Robertson v. Bucklen, 107 Ill. App. 369	715	Scovill v. Thayer, 105 U. S. 143	622, 639, 785, 842
Robinson v. National Bank, 95 N. Y. 637	744, 749	Screven Hose Co. v. Philpot, 53 Ga. 625	294
Robotham v. Prudential Ins. Co., 64 N. J. Eq. 673	215, 501	Searles v. Gebbie, 115 App. Div. (N. Y.) 778	566
Rochester & Kettle Falls Land Co. v. Raymond, 158 N. Y. 576	898	Searsburgh Turnpike Co. v. Cutler, 6 Vt. 315	182
Roedde v. News-Advertiser Pub. Co., 4 British Columbia 7	224	Sears v. Kings County &c. R. Co., 152 Mass. 151	454
Rogers v. Nashville &c. R. Co., 91 Fed. 299	521	Seaton v. Grant, L. R. 2 Ch. App. 459	689
v. Pell, 154 N. Y. 518	229, 428	Sedalia &c. R. Co. v. Wilkerson, 83 Mo. 235	370, 371
Rollins v. Denver Club, 43 Colo. 345	578	Sellers v. Greer, 172 Ill. 549	3
Rothchild v. Memphis &c. R. Co., 113 Fed. 476	684, 722	Senior v. New York City R. Co., 111 App. Div. (N. Y.) 39	52
Rough v. Breitung, 117 Mich. 48	11	Senn v. Union Premium Mercantile Co., 115 Mo. App. 685	729
Rouse v. Merchants' Nat. Bank, 46 Ohio St. 493	794	Seymour v. Chicago &c. Life Society, 54 Minn. 147	313
Rowell v. Janvrin, 151 N. Y. 60	901	Shattuck v. American Cement Co., 205 Pa. 197	766
Roy & Co. v. Scott, Hartley & Co., 11 Wash. 399	501	Shaw v. Davis, 78 Md. 308	710

[References are to Pages.]

Shaw v. Quincy Mining Co., 145 U. S.	81	South Dakota v. North Carolina, 192 U. S.	360
444		286	
v. R. R. Co., 101 U. S.	567	South Georgia &c. R. Co. v. Ayres, 56 Ga.	416
v. Staigh, 107 Minn.	665, 699	230	
Shea v. Mabry, 1 Lea (Tenn.)	319	South Joplin Land Co. v. Case, 104 Mo.	920
Sheldon v. Chappel, 47 Hun (N. Y.)	232	572	
59		South Milwaukee Co. v. Murphy, 112 Wis.	886
Sheldon Hat Blocking Co. v. Eickemeyer &c. Mach. Co., 90 N. Y.	607	614	
59, 683		South-Western R. Co. v. Thomason, 40 Ga.	108
Shenandoah Valley R. Co. v. Griffith, 76 Va.	913	408	
757		Spear v. Crawford, 14 Wend. (N. Y.)	360
Shepard Voting Trust Cases, 60 Conn.	540	20	
553		Spencer v. Champion, 9 Conn.	535
Sheridan Elec. Light Co. v. Chatham Nat. Bank, 127 N. Y.	517	Sperring's Appeal, 71 Pa. St.	11
Sherman v. Fitch, 98 Mass.	59	490	
Sherwood v. American Bible Society, 4 Abh. App. Dec. (N. Y.)	227	Spokane v. Amsterdam Trustees Kan- toor, 22 Wash.	172
Shields v. Hobart, 172 Mo.	491	Sprague v. Illinois &c. R. Co., 19 Ill.	420
Shipman v. Treadwell, 200 N. Y.	472	174	
Shively v. Eureka &c. Min. Co., 5 Cal.	457	v. National Bank of America, 172 Ill.	858
App. 236		149	
Shoemaker v. Washburn Lumber Co., 97 Wis.	585	Spring Co. v. Knowlton, 103 U. S.	49
211		Springfield &c. Threshing Co. v. Green, 25 Ill. App.	106
Sigman v. Electric Vehicle Co., 140 Fed.	117	13	
701		Spring Valley Water Works v. San Francisco, 22 Cal.	434
Simm v. Anglo-American Telegraph Co., 5 Q. B. D.	188	Squair v. Lookout Mtn. Co., 42 Fed.	665
Sims v. Petaluma Gas Light Co., 131 Cal.	656	729	
494		Squire v. Princeton Lighting Co., 72 N. J. Eq.	883
Sinclair v. Fuller, 158 N. Y.	607	789	
Stank v. Andrews, 57 N. Y.	133	Stacy v. Glen Ellyn Hotel &c. Co., 223 Ill.	546
Stack v. North Western Nat'l Bk., 103 Wis.	57	233	
812		Stanwood v. Sterling Metal Co., 107 Ill. App.	569
Slater Woolen Co. v. Lamb, 143 Mass.	420	566	
300		Stark Bank v. United States Pottery Co., 34 Vt.	144
Slee v. Bloom, 5 Johns. Ch. (N. Y.)	366	Starkey v. Bank of England, (1903) A. C.	114
946		779	
v. Bloom, 19 Johns. (N. Y.)	456	Starkweather v. American Bible So- ciety, 72 Ill.	50
Slocum v. Head, 105 Wis.	431	232	
v. Providence &c. Pipe Co., 10 R. I.	112	665	
168		Starr v. Shepard, 145 Mich.	302
v. Warren, 10 R. I.	116	271	
168		93	
Smith v. Burns &c. Mfg. Co., 132 Wis.	177	v. Atchison &c. Pub. Co., 3 Lea (Tenn.)	729
363, 413		22	
v. Gower, 63 Ky.	17	v. Baltimore &c. R. Co., 15 W. Va.	362
v. Hurd, 12 Metc. (Mass.)	371	22	
v. Kellogg, 194 N. Y.	567	v. Baltimore &c. R. Co., 120 Ind.	298
v. New York &c. R. Co., 96 Fed.	504	22	
146		v. Creamery Package Mfg. Co., 110 Minn.	415
v. San Francisco &c. R. Co., 115 Cal.	584	59	
523		v. Dawson, 16 Ind.	40
v. Silver Valley Min. Co., 64 Md.	85	State v. Higby Co., 130 Iowa	69
115		232	
v. Smith, 62 Ill.	493	v. Janesville Water Power Co., 92 Wis.	496
544		639	
v. Wells Mfg. Co., 148 Ind.	333	729	
444, 501		v. McIver, 2 S. Car.	25
Snediker v. Ayres, 146 Cal.	407	v. Minn. Thresher Mfg. Co., 40 Minn.	213
Sneider's Sons Co. v. Troy, 91 Ala.	224	639	
Snook v. Georgia Improvement Co., 83 Ga.	61	v. Morris &c. R. Co., 23 N. J. L.	360
420		22	
Societe Generale De Paris v. Walker, L. R.	11 App. Cas.	v. Oberlin &c. Loan Assn., 35 Ohio St.	258
744		544	
Society of Practical Knowledge v. Abbott, 2 Beav.	559	v. Overton, 24 N. J. L.	435
South &c. R. Co. v. Chappell, 61 Ala.	527	v. Passaic Co. Agr. Society, 54 N. J. L.	260
353		22	
Southern Exp. Co. v. Platten, 93 Fed.	936	v. Pittsburg &c. R. Co., 68 Ohio St.	9
22		233	
v. State, 1 Ga. App.	700	v. Smith, 48 Vt.	266
Southern Ry. Co. v. Allison, 190 U. S.	126	581, 729	
22		v. Stockley, 45 Ohio St.	304
v. State, 125 Ga.	287	523	
South Bend Chilled Plow Co. v. George C. Cribb Co., 97 Wis.	230	v. Trustees of Vincennes Univer- sity, 5 Ind.	77
815		944	
South Buffalo Natural Gas Co. v. Bain, 9 Misc. (N. Y.)	425	v. U. S. &c. Trust Co., 140 Ala.	710
384		950	
		v. Webb, 97 Ala.	111
		639	
		v. Western Irrigating Canal Co., 40 Kans.	96
		119	
		v. White, 96 Mo. App.	34
		23	
		v. Woolen Mills Co., 115 Tenn.	266
		944	
		State Bank v. State, 1 Blackf. (Ind.)	267
		964	

[References are to Pages.]

United States Vinegar Co. v. Foehrenbach, 148 N. Y. 58	387, 416	Wechselburg v. Flour City Nat. Bank, 64 Fed. 90	167
Uley v. Union Tool Co., 11 Gray (Mass.) 139	168	Weckler v. First Nat. Bank, 42 Md. 581	347
V			
Van Allen v. Assessors, 3 Wall. (U. S.) 573	113	Weigand v. Alliance Supply Co., 44 W. Va. 133	945
Van Buren v. Reformed Church, 62 Barb. (N. Y.) 495	168	Weir v. Bay State Gas Co., 91 Fed. 940	665
Vance v. McNabb & Co. Coal Co., 92 Tenn. 47	28	Wellington & Co. R. Co. v. Cashie & Lumber Co., 114 N. Car. 690	184
v. Phoenix Ins. Co., 4 Lea (Tenn.) 385	490	Wells v. Cowles, 2 Conn. 567	108
Van Cleve v. Berkey, 143 Mo. 109	858	v. Green Bay & Co. Canal Co., 90 Wis. 442	639
Van Cott v. Van Brunt, 82 N. Y. 535	852	Welton v. Saffery, A. C. (1897) 299	625
Vanderpoel v. Gorman, 140 N. Y. 563	232, 812	Wemple v. St. Louis & Co. R. Co., 120 Ill. 196	359
Van Etten v. Eaton, 19 Mich. 187	122	Wendler Mach. Co., Matter of, 2 App. Div. (N. Y.) 16	428
Van Schaick v. Mackin, 129 App. Div. (N. Y.) 335	356	Werle v. Northwestern Flint & Sand-paper Co., 125 Wis. 534	229
Van Weel v. Winston, 115 U. S. 228	809	West Chester & Co. R. Co. v. Jackson, 77 Pa. St. 321	602
Vaughn v. Alabama Nat. Bank, 143 Ala. 572	785	Westcott v. Fargo, 61 N. Y. 542	93
Venable Bros. v. Southern Granite Co., 135 Ga. 508	958	West End Real Estate Co. v. Nash, 51 W. Va. 341	413
Venner v. Atchison & Co. R. Co., 28 Fed. 581	428	Western & Co. Mfg. Co. v. Cousley, 72 Ill. 531	929
Vicksburg & Co. Railroad v. McKean, 12 La. Ann. 638	384	Western & Co. R. Co. v. Blue Ridge Hotel Co., 102 Md. 307	232
Vidal v. Girard's Exrs., 2 How. (U. S.) 127	232	Wetherbee v. Baker, 35 N. J. Eq. 501	789
Von Arnim v. American Tube-Works, 188 Mass. 515	684	West Nashville Planing-Mill Co. v. Nashville Savings Bk., 86 Tenn. 252	901
Vredenburg v. Behan, 33 La. Ann. 627	182	Weston Elec. Inst. Co. v. Empire Elec. Inst. Co., 177 Fed. 1006	39
W			
Wabash Railroad Co. v. Dougan, 142 Ill. 248	140	Wheeler v. Everett Land Co., 14 Wash. 630	232
Waggoner-Gates Milling Co. v. Ziegler-Zaiss Commission Co., 128 Mo. 473	794	v. Millar, 90 N. Y. 353	360
Wallace v. Townsend, 43 Ohio St. 537	371	v. Northwestern Sleigh Co., 39 Fed. 347	573
Wallamet Falls & Co. v. Kittredge, 5 Sawy. (U. S.) 44	948	Wickersham v. Crittenden, 93 Cal. 17	499
Wallerstein v. Ervin, 112 Fed. 124	224	Wight v. Shelby R. Co., 16 B. Mon. (Ky.) 4	384
Walsh v. Goulden, 130 Mich. 531	514	Wilks v. Georgia Pacific R. Co., 79 Ala. 180	309
Walworth v. Brackett, 98 Mass. 98	132	Willard v. Holmes, 142 N. Y. 492	13
Warburton v. Trust Co., 158 Fed. 969	939	Williams v. Citizen's Enterprising Co., 153 Ind. 496	387
Ward v. Davidson, 89 Mo. 445	451	v. Hewitt, 47 La. Ann. 1076	167
v. Joslin, 186 U. S. 142	864	v. Ingersoll, 89 N. Y. 508	757
v. Minnesota & Co. R. Co., 119 Ill. 287	184	v. McDonald, 42 N. J. Eq. 392	464
Warner v. Penoyer, 91 Fed. 587	491	v. Montgomery, 148 N. Y. 519	531
Warren v. King, 108 U. S. 389	619	Williamson v. Kokomo & Co. Fund Assn., 89 Ind. 389	184
v. Pinn, 65 N. J. Eq. 36	539	Willoughby v. Chicago Junction Railways & Co., 50 N. J. Eq. 656	696
Wasburn v. Nat. Wall-Paper Co., 81 Fed. 17	859	Wilson v. Leary, 120 N. Car. 90	964
Washington Life Ins. Co. v. Clason, 162 N. Y. 305	309	Wincham Shipbuilding & Co., L. R. 9 Ch. Div. 322	812
Washington Savings Bk. v. Butchers' & Drovers' Bk., 130 Mo. 155	785	Windmuller v. Standard & Co. Distributing Co., 115 Fed. 748	722
Waterhouse v. Jamieson, L. R. 2 H. L. (Sc.) 29	902	Windsor Elec. Light Co. v. Tandy, 66 Vt. 248	396
Waterman v. Chicago & Co. R. Co., 139 Ill. 658	451	Wing v. Slater, 19 R. I. 597	864
Waters v. Taylor, 15 Ves. 10	432	Winget v. Quincy Building & Co. Assn., 128 Ill. 67	175
v. Waters & Co., 201 N. Y. 184	673	Winston v. Dorsett & Co. Paving Co., 129 Ill. 64	406
Watertown Paper Co., In re, 169 Fed. 252	46	v. Dorsett Pipe & Paving Co., 129 Ill. 64	625
Waycross Air-Line R. Co. v. Offerman & Co. R. Co., 109 Ga. 827	46	Winterfield v. Cream City Brewing Co., 96 Wis. 239	232
Weatherford & Co. R. Co. v. Granger, 86 Tex. 350	932	Wintner v. Rosemont Realty Co., 101 App. Div. (N. Y.) 30	929
Weaver v. Barden, 49 N. Y. 286	766	White v. Howard, 38 Conn. 342	232
		v. President & Co. of Franklin Bank, 22 Pick. (Mass.) 181	331
		White Star Line v. Star Line, 141 Mich. 604	222

Whittaker v. Amwell Nat. Bk., 52 N. J. Eq. 400	557		
Whittenton Mills v. Upton, 10 Gray (Mass.) 582	222		
Witherbee v. Bowles, 201 N. Y. 427	699		
Wolf v. Pennsylvania R. Co., 195 Pa. St. 91	707		
Wood v. Dummer, 3 Mason (U. S.) 305	783		
v. Whelen, 93 Ill. 153	428		
Woodberry v. McClurg, 78 Miss. 831	218		
Wood Harvester Co. v. Robbins, 56 Minn. 48	396		
Woodroof v. Howes, 88 Cal. 184	715		
Woods Motor Vehicle Co. v. Brady, 181 N. Y. 145	413		
Wormser v. Metropolitan Street R. Co., 184 N. Y. 83	688		
Wright v. Hughes, 119 Ind. 324	313		
Wright v. Pipe Line Co., 101 Pa. St. 204	313		
Wuller v. Chuse Grocery Co., 241 Ill. 398	359		
		Y	
		Yale Gas Stove Co. v. Wilcox, 64 Conn. 101	920
		Yates v. Jones Nat. Bank, 206 U. S. 158	464, 822
		Yonkers Gazette Co. v. Taylor, 30 App. Div. (N. Y.) 334	382, 414
		Young v. Columbia Land & Investment Co., 53 Ore. 438	707
		v. Naval &c. Society, Ltd., 1 K. B. 687	457
		Z	
		Zelaya Min. Co. v. Meyer, 8 N. Y. S. 487	628
		Zinc Carbonate Co. v. First Nat. Bank, 103 Wis. 125	353

CASES ON PRIVATE CORPORATIONS

CHAPTER I.

THE LEGAL CONCEPTION OF A CORPORATION.

Section 1.—Considered in its Relation to Non-Members.

Co. Lit. 250 a. "Bodies politike, &c. This is a body to take in succession, framed (as to that capacity) by policie, and thereupon it is called here by Littleton a body politike; and it is also called a corporation, or a body incorporate, because the persons are made into a body, and are of capacity to take and grant, &c. * * * Every body politike, or corporate is either ecclesiasticall or lay. * * * And again it is either sole, or aggregate of many. And this body politike, or corporate, aggregate of many, is by the civilians called *collegium* or *universitas*."

1 Bl. Com., 467-8. "But as all personal rights die with the person; and, as the necessary forms of investing a series of individuals, one after another, with the same identical rights, would be very inconvenient, if not impracticable; it has been found necessary, when it is for the advantage of the public to have any particular rights kept on foot and continued, to constitute artificial persons, who may maintain a perpetual succession, and enjoy a kind of legal immortality.

These artificial persons are called bodies politic, bodies corporate, (*corpora corporata*), or corporations: of which there is a great variety subsisting, for the advancement of religion, of learning, and of commerce; in order to preserve entire and forever those rights and immunities, which, if they were granted only to those individuals of which the body corporate is composed, would upon their death be utterly lost and extinct. * * * When they are consolidated and united into a corporation, they and their successors are then considered as one person in law: as one person, they have one will, which is collected from the sense of the majority of individuals: * * * The privileges and immunities, the estates and possession, of the corporation, when once vested in them, will be forever vested, without any new conveyance to new succession; for all the individual members that have existed from the foundation to the present time, or that shall ever hereafter exist, are but one person in law, a

person that never dies: in like manner as the river Thames is still the same river, though the parts which compose it are changing every instant."

ERICKSON v. REVERE ELEVATOR CO.

1910. 110 Minn. 443, 126 N. W. 130.

ACTION in the district court for Redwood county to recover \$3,161.45, which plaintiff had been compelled to pay upon a promissory note which he had signed as surety for defendant. The substance of the complaint and of the defense is given in the opinion. From an order, Olsen, J., sustaining plaintiff's demurrer to the defense set up in the answer on the ground it did not state facts sufficient to constitute a defense, and sustaining plaintiff's demurrer to the counterclaim on the ground it did not state facts sufficient to constitute a counterclaim, defendant appealed. Affirmed.

O'BRIEN, J.—According to the complaint, on September 14, 1903, defendant delivered to Minnesota Grain Company its promissory note for \$6,000, payable on or before one year from date. Plaintiff signed the note as a surety, and on March 11, 1909, was compelled to pay a balance of \$3,161.45, remaining unpaid, and brought this action to recover that amount. Defendant served an answer containing general and special denials, and alleging as a separate defense that on May 21, 1907, N. H. Dahl, A. O. Anderson, C. O. Nichols, E. L. Nelson, and the plaintiff were owners of the entire capital stock of defendant, and on said date, through N. H. Dahl, their duly constituted agent, sold their entire holdings to Charles Gamble, Martha Anderson, A. G. Anderson, F. J. Sheffield, and K. E. Mo for \$7,500, upon a statement representing and warranting "that the said corporation was free from debts and every and all obligations," and "that there were no liens, encumbrances, or indebtedness of any kind against said corporation or any of its said property." In reliance upon the representations those named purchased and still own all the stock. Therefore it is claimed the plaintiff is estopped. The same allegations are reasserted for damages as a counterclaim or set-off. Plaintiff demurred to the allegations of affirmative defense. This appeal is from an order sustaining the demurrer.

There can be no doubt that, if the allegations of the answer are true, there must be some procedure by which the stockholders, who are the beneficial owners of the defendant corporation and its property, can be protected. But we do not think this demurrer can be overruled without violating the fundamental principles underlying the creation and legal status of corporations. (It is true that where the corporate form is used by individuals for the purpose of evading the law, or for the perpetration of fraud, the court will not permit the legal entity to be interposed so as to defeat justice.) The necessity for this rule is becoming more apparent each day, not only in the maintenance of private rights, but for the preservation of public

rights in the regulation and necessary control of large corporations. *State v. Creamery Package Mfg. Co.*, supra, page 415, 126 N. W. 126, and cases cited. But in ordinary business transactions, and for the purpose of determining the respective rights, responsibilities, and powers of corporations, its officers, stockholders, and those dealing with them, it is necessary that the distinction between the corporation, as a legal entity, and its members, be strictly maintained.

The note sued upon was not a debt of the original stockholders, but of the corporation. The sale of the stock was not a corporate act, but that of the individual stockholders. [A stockholder in his individual capacity, or any number of stockholders, cannot bind the corporation in its corporate capacity, except under the extraordinary circumstances already referred to.] The sale of the stock, therefore, in no manner affected the liability of the corporation upon the note, and the corporation itself, considered as a distinct entity, cannot avail itself of the rights of its present stockholders possessed by them as individuals. *Gallagher v. Germania Brewing Co.*, 53 Minn. 214, 54 N. W. 1115. Notwithstanding this, a stockholder has a direct and real interest in the property of the corporation, and may, when the corporation will not or cannot fully protect its property, be recognized as a proper party to prosecute or defend an action involving primarily the corporation's rights. *Baldwin v. Canfield*, 26 Minn. 43, 1 N. W. 261, 276.

The difficulty here is that the corporation is attempting to assert a defense which is personal to the individual stockholders, who are not parties to the action, and who are at liberty at any time to dispose of their stock holdings, a transaction which would not transfer to the purchaser the rights relied upon in the answer. If we had before us a demand upon the part of the individual stockholders to be allowed to intervene and protect their interests in this action, it would be a different question, and one upon which we express no opinion. *Becker v. Northway*, 44 Minn. 61, 46 N. W. 210, 20 Am. St. 543.

Order affirmed.¹

PEOPLE'S PLEASURE PARK CO. ET AL. v. ROHLEDER.

1908. 109 Va. 439, 61 S. E. 794, 63 S. E. 981.

APPEAL from a decree of the Circuit Court of Henrico county. Decree for complainant. Defendants appeal.

¹"Whenever a corporation makes a contract, it is the contract of the legal entity: of the artificial being created by the charter; and not the contract of the individual members." Taney, C. J., in *Bank of Augusta v. Earle* (1839) 13 Pet. (U. S.) 519, 587, 10 L. ed. 274.

See also *Moore & Co. Hardware Co. v. Towers Hardware Co.* (1888) 87 Ala. 206; *Sellers v. Greer* (1898) 172 Ill. 549, 50 N. E. 246; *Gallagher v. Germania Brewing Co.* (1893) 53 Minn. 214, 54 N. W. 1115.—Eds.

The opinion states the case:

CARDWELL, J., delivered the opinion of the court.

Appellee filed her bill against appellants, the purposes thereof being to annul a conveyance of certain lands located in Henrico county, and known as Fulton Park, to appellant, People's Pleasure Park Company, Inc., from its co-appellants, Ida M. Butts and D. G. Fulton, and perpetually to enjoin and restrain the People's Pleasure Park Company, Inc., from selling or otherwise disposing of the said property, or any part thereof, to colored persons for any purpose whatsoever, or to any person for the purpose of using the same as a public park or place of amusement for colored persons.

It is averred that in the year 1900, Bliss Black and wife acquired from the heirs of one Samuel Mosby, deceased, title to a tract of about 125 acres of land in Henrico county, near Fair Oaks Station, at the junction of the Southern Railway with the electric railway running from Richmond City to Seven Pines, and platted the same, under the name of Fulton Park, into 1,330 lots, recording a small part of the plat—105 lots—in Henrico county clerk's office; that between the date of said purchase and the beginning of the controversy out of which this litigation arises, there were a number of conveyances of said tract of land (except the small number of lots that had been sold therefrom), but these conveyances were to parties who either represented the Blacks, or were identical in interest with them; that it was the original intention of the Blacks to establish a settlement of white persons at Fulton Park, and representations were made to that effect by them, both in oral statement when trying to sell lots and in published advertisements of the lots for sale in newspapers, in printed handbills posted, etc.; that about thirty, only, of the lots were sold by the Blacks or their associates, of three of which, with a small dwelling thereon, appellee, on October 5, 1904, became the owner, having purchased the same for a home from Harriet J. Powers, who took from Ida M. Butts during the time that the latter held title to all the lots in Fulton Park, except such of them as had been previously sold and conveyed by her or the Blacks; that in the deed to Harriet J. Powers, appellee's grantor, there was the covenant, condition, or stipulation in these words: "The title to this land never to vest in a person or persons of African descent"—and the deed to appellee was made subject to the limitations and restrictions contained in the deed to Harriet J. Powers.

It is further averred that, after the title to the remaining land (Fulton Park) had again been acquired by Black and wife, they conveyed it as a whole to the Revere Beach County Fair and Musical Railway Company, excepting the lots previously sold, and in this conveyance is the covenant, condition and stipulation: "The title to this land never to vest in a colored person or persons"—that afterward the Revere Beach County Fair and Musical Company transferred the property to one Jessie M. Smith, providing in the deed that the same should be subject to the covenant, condition, or

stipulation imposed thereon by Black in his deed to the company; that, after Jessie M. Smith had held the property a few months, she transferred the title thereto by a conveyance from herself as an individual to herself as trustee without specifying the nature of the trust or naming the beneficiary or beneficiaries thereof, and omitting mention of the "covenant, condition, or stipulation" under which she had held the property, as an individual; that Jessie M. Smith, as trustee, but without disclosing the nature of the trust or the beneficiary or beneficiaries thereof, conveyed the property again to Ida M. Butts, trustee, making no mention of a restriction upon the latter's power to alienate the property, or as to whom she might convey it; and that on or about May 3, 1906, a deed was recorded in the clerk's office of Henrico county, by which all the unsold portion of Fulton Park was conveyed by Ida M. Butts to one D. G. Fulton, who by deed recorded in the same office, on the same day, conveyed the property to appellant, People's Pleasure Park Co., Inc. The bill then charges that the People's Pleasure Park Co. is a corporation composed exclusively of negroes, and that this corporation purchased Fulton Park for the express purpose of converting the same into a park or place of amusement for colored people; that the corporation, before it purchased the property, was fully apprised of the "condition, covenant, or stipulation" theretofore in the bill mentioned as having been incorporated in the deed conveying the property to the Revere Beach County Fair and Musical Co., and also aware of the pendency of injunction proceedings to prevent said appellant from acquiring title to Fulton Park. * * *

Aside from the question whether or not appellee could obtain the relief she asks against appellants—that is, an annulment of the conveyance to appellant, People's Pleasure Park Co., Inc.,—on the ground that the restriction on the right of alienation of any of the Fulton Park land to "a person or persons of African descent" or "colored person" had been violated by a sale of a part of the land to said appellant, the bill fails to allege facts showing a violation of the restriction, and should have been dismissed upon the demurrers thereto. Such a conveyance, by no rule of construction, vests the title to the property conveyed in "a person or persons of African descent." Although a copy of the charter of the grantee is filed as an exhibit with the bill and made a part thereof, and which sets out that the object for which the corporation is formed is "to establish and develop a pleasure park for the amusement of colored people," a contemplated sale of the property to "a person or persons of African descent" is not even alleged, but only a contemplated use of the property as a place of amusement for colored persons, which the restriction relied on neither expressly, nor by implication, prohibits.

"A corporation is an artificial person, like the state. It has a distinct existence—an existence separate from that of its stockholders and directors." 1 Cook on Corp. (4th ed.), sec. 1.

Prof. Rudolph Sohm, in his *Institutes of Roman Law*, pp. 104-106, says: "In Roman law the property of the corporation is the sole property of the collective whole; and the debts of a corporation are the sole debts of the collective whole. * * * It represents a kind of ideal private person, an independent subject capable of holding property, totally distinct from all previously existing persons, including its own members. It possesses, as such, rights and liabilities of its own. It leads its own life, as it were, quite unaffected by any change of members. It stands apart as a separate subject or proprietary capacity, and, in contemplation of law, as a stranger to its own members. The collective whole, as such, can hold property. Its property, therefore, is, as far as its members are concerned, another's property, its debts another's debts. * * * Roman law contrived to accomplish a veritable masterpiece of juristic ingenuity in discovering the notion of a collective person; in clearly grasping and distinguishing from its members the collective whole as the ideal unity of the members bound together by the corporate constitution; in raising this whole to the rank of a person (a juristic person, namely), and in securing it a place in private law as an independent subject of proprietary capacity standing on the same footing as other private persons."

MARSHALL, C. J., in the *Dartmouth College Case*, 4 Wheat. (U. S.) 518, 4 L. Ed. 629, defined a corporation as, "an artificial being, invisible, intangible, and existing only in contemplation of law."

In *Green's Brice, Ultra Vires* (2d Am. ed.), secs. 1, 2, it is said that "a corporation is a person which exists in contemplation of law only, and not physically."

The same author, in commenting on Kyd's definition, says: "But sufficient stress is not laid upon that which is its real characteristic in the eye of the law, viz., its existence separate and distinct from the individual or individuals composing it. * * * This is the one important fact. The members of a corporation aggregate, and the one individual who is constituted a corporation sole, may, from their connection with such, have rights and privileges, and be under obligations and duties, over and above those affecting them in their private capacity; but they get them by reflection, as it were, from the corporation. They individually are not the corporation—cannot exercise the corporate powers, enforce the corporate rights, or be responsible for the corporate acts."

In *Stewart & Palmer v. Thornton*, 75 Va. 215, the syllabus of the case is as follows: "The county school boards are, by act of assembly, constituted a corporation, and a suit to recover a fund belonging to the corporation must be brought in its corporate name. A suit by persons styling themselves the directors of the county school board of their county cannot be maintained." In the opinion by Burks, J., referring to the rule that a corporation must sue and be sued by its corporate name, it is said: "Like a natural person 'it is recognized in law only by its name, and in its corporate capacity,

rights and liabilities, it is as distinct from the persons composing it as an incorporated city is from an inhabitant of the city.' " Further recognizing the corporation as a legal entity distinct from the persons composing it, the opinion in that case quotes from Judge Denio, in *People v. Fulton*, 11 N. Y. Rep. 94, as follows: "Incorporated religious societies are aggregate corporations, and whatever property they acquire, whether it be real or personal, is vested in interest in the body corporate; and, while the officers have it under their control or dominion, whatever possession they have is the possession of the artificial person whose agents they are. Although called trustees, they do not hold the property in trust for the corporation or the religious society. The name is simply the title of their office, and their position respecting the corporate property would be the same if they were denominated directors or managers. Their right to intermeddle is an authority, and not an estate, or title. They have no other possession than the directors of a bank have of the banking house. This would be so *upon general principles relating to the legal nature of corporations*, apart from the particular language of the act concerning religious corporations."

For the above reasons, we are of opinion that the decree complained of is erroneous, and it will be set aside and annulled, the demurrers of appellants to the bill sustained, and the bill dismissed with costs to the appellants.

*Reversed.*²

BUTTON v. HOFFMAN.

1884. 61 Wis. 20, 20 N. W. 667.

APPEAL from the Circuit Court for Jackson County.

Replevin. The facts sufficiently appear from the opinion. The defendant appealed from a judgment in favor of the plaintiff.

ORTON, J.—This is an action of replevin in which the title of the plaintiff to the property was put in issue by the answer.

In his instructions to the jury the learned judge of the circuit court said: "I think the testimony is that the plaintiff had the title to the property." The evidence of the plaintiff's title was that the

² A British statute forbade the registration of any vessel owned by foreigners "in whole or in part, directly or indirectly." A corporation chartered by Great Britain, some of whose stockholders were foreigners, sought to compel the registry of its vessel. *Held*, "the British corporation is to all intents the legal owner of the vessel, and entitled to the registry," for "~~in no legal sense are the individual members the owners.~~" *Queen v. Arnand* (1846) 9 Q. B. (Adol. & El.) 806. To similar effect, *Foster & Son Limited v. Commissioners of Inland Revenue*, L. R. (1894) 1 Q. B. 516; *Syndicate Ins. Co. v. Bohn* (1894) 65 Fed. 165, 169; *Humphreys v. McKissock* (1890) 140 U. S. 304, 35 L. ed. 473.

See articles, "Corporate Personality", by Arthur W. Machen, Jr., 24 Harv. Law Rev. 253, 347.—Eds.

property belonged to a corporation known as "The Hayden & Smith Manufacturing Company," and that he purchased and became the sole owner of all of the capital stock of said corporation. As the plaintiff in his testimony expressed it, "I bought all the stock. I own all the stock now. I became the absolute owner of the mill. It belonged at that time to the company, and I am the company." There was no other evidence of the condition of the corporation at the time. Is this sufficient evidence of the plaintiff's title? We think not. The learned counsel of the respondent in his brief says: "The property had formerly belonged to the Hayden & Smith Manufacturing Company, but the respondent had purchased and become the owner of all the stock of the company, and thus became its sole owner."

From the very nature of a private corporation, or, indeed, of any corporation, the stockholders are not the private and joint owners of its property. The corporation is the real, though artificial, person substituted for the natural persons who procured its creation and have pecuniary interests in it, in which all its property is vested, and by which it is controlled, managed and disposed of. It must purchase, hold; grant, sell and convey the corporate property, and do business, sue and be sued, plead and be impleaded, for corporate purposes, by its corporate name. The corporation must do its business in a certain way, and by its regularly appointed officers and agents, whose acts are those of the corporation only as they are within the powers and purposes of the corporation. In an ordinary co-partnership the members of it act as natural persons and as agents for each other, and with unlimited liability. But not so with a corporation; its members, as natural persons, are merged in the corporate identity. *Ang. & A. on Corp.*, secs. 40, 46, 100, 591, 595. A share of the capital stock of a corporation is defined to be a right to partake, according to the amount subscribed, of the surplus profits obtained from the use and disposal of the capital stock of the company to those purposes for which the company is constituted. *Id.*, sec. 557. The corporation is the trustee for the management of the property, and the stockholders are the mere *cestuis que trust*. *Gray v. Portland Bank*, 3 Mass. 365; *Eidman v. Bowman*, 4 Am. Corp. Cas. 350. The right of alienation or assignment of the property is in the corporation alone, and this right is not affected by making the stockholders individually liable for the corporate debts. *Ang. & A. on Corp.*, sec. 191; *Pope v. Brandon*, 2 Stewart (Ala.) 401; *Whitwell v. Warner*, 20 Vt. 444. The property of the corporation is the mere instrument whereby the stock is made to produce the profits, which are the dividends to be declared from time to time by corporate authority for the benefit of the stockholders, while the property itself, which produces them, continues to belong to the corporation. *Bradley v. Holdsworth*, 3 Mees. & W. 422; *Waltham Bank v. Waltham*, 10 Met. 334; *Tippets v. Walker*, 4 Mass. 595. The corporation holds its property

only for the purposes for which it was permitted to acquire it, and even the corporation cannot divert it from such use, and a shareholder has no legal right to it, or the profits arising therefrom, until a lawful division is made by the directors or other proper officers of the corporation, or by judicial determination. *Ang. & A. on Corp.*, secs. 160, 190, 557; *Hyatt v. Allen*, 4 *Am. Corp. Cas.* 624. A conveyance of all the capital stock to a purchaser gives to such purchaser only an equitable interest in the property to carry on business under the act of incorporation and in the corporate name, and the corporation is still the legal owner of the same. *Wilde v. Jenkins*, 4 *Paige* 481. A legal distribution of the property after a dissolution of the corporation and settlement of its affairs, is the inception of any title of a stockholder to it, although he be the *sole* stockholder. *Ang. & A. on Corp.*, sec. 779a.

These general principles sufficiently establish the doctrine that the owner of all the capital stock of a corporation does not therefore own its property, or any of it, and does not himself become the corporation, as a natural person, to own its property and do its business in his own name. While the corporation exists he is a mere stockholder of it, and nothing else. The consequences of a violation of these principles would be that the stockholders would be the private and joint owners of the corporate property, and they could assume the powers of the corporation, and supersede its functions in its use and disposition for their own benefit without personal liability, and thus destroy the corporation, terminate its business, and defraud its creditors. The stockholders would be the owners of the property, and, at the same time, it would belong to the corporation. One stockholder owning the whole capital stock, could, of course, do what several stockholders could lawfully do. It is said in *Utica v. Churchill*, 33 *N. Y.* 161, "the interest of a stockholder is of a collateral nature, and is not the interest of an owner;" and in *Hyatt v. Allen*, *supra*, that "a shareholder in a corporation has no legal title to its property or profits until a division is made." In *Winona & St. P. R. R. Co. v. St. P. & S. C. R. R. Co.*, 23 *Minn.* 359, it is held that the corporation is still the absolute owner, and vested with the legal title of the property, and the real party in interest, although another party has become the owner of the sole beneficial interest in its rights, property and immunities. In *Baldwin v. Canfield*, 26 *Minn.* 43, it was held that the sole owner of the stock did not own the land of the corporation so as to convey the same. In *Bartlett v. Brickett*, 14 *Allen* 62, an action of replevin was brought by A, B, and C, as the "Trustees of the Ministerial Fund in the North Parish in Haverhill," which was the corporate name. In portions of the writ the plaintiffs were referred to as "the said trustees" and "the said plaintiffs." In the bond, "A, B, and C, trustees as aforesaid," became bound, and the officer, in his return, certified that he had taken a bond "from the within-named A, B, and C," and the property was received by "A, B, and C, plaintiffs." It was held that the action was

not by the corporation, as it should have been, and judgment was rendered for the defendant. It is said in *Van Allen v. Assessors*, 3 Wall. 584, "the corporation is the legal owner of all the property of the bank, both real and personal." In *Wilde v. Jenkins*, supra, where a co-partnership bought all the property and effects, together with the franchises, of a corporation, and elected themselves trustees of the corporation, it was held that the corporation was not dissolved, and that the legal title to the real and personal property was still in the corporation for their benefit. In *Mickles v. R. C. Bank*, 11 Paige 118, it was held that, although a corporation was deemed to have surrendered its charter for a nonuser, it was not dissolved, and would not be until its dissolution was judicially declared, and that until then its property could be taken and sold by its judgment creditors. In *Bennett v. Am. Art Union*, 5 Sandf. Super. Ct. 614, it was held that, "as a general rule, the whole title, legal and equitable (to its property), is vested in the corporation itself," and that the individual members have no other or greater interest in it than is expressly given to them by the charter, and the prayer of the complainant, as a shareholder in the Art Union, for an injunction against a certain disposition of its property, was denied, because he had no interest in it. See also, *Goodwin v. Hardy*, 57 Me. 143.

It is true that none of the above cases are precisely parallel with the present case in facts, but they are sufficiently analogous to be authority upon the principle that the plaintiff, as the sole stockholder of the corporation, is not the legal owner of its property. He may have an equitable interest in it, but in this action he must show a legal title to the property in himself in order to recover, and he has shown that such title is in another person. *Timp v. Dockham*, 32 Wis. 146; *Sensenbrenner v. Mathews*, 48 Wis. 250. In analogy to the above principle it was held in *Murphy v. Hanrahan*, 50 Wis. 485, that the sole heirs of an estate did not have such a legal title to a promissory note given to their father as would entitle them to sue the maker upon it, because the title to it was in the administrator, and they could obtain the title only by administration and distribution according to law. The heirs in that case certainly had as much equitable interest in that note as this plaintiff has in the property in controversy. The want of title to the property being fatal to the plaintiff's recovery in the action between the present parties, other alleged errors will not be considered.

By the Court.—*The judgment of the circuit court is reversed, and the cause remanded for a new trial.*³

³ *Spencer v. Champion* (1833) 9 Conn. 535; *Newton Mfg. Co. v. White* (1871) 42 Ga. 148; *Exchange Bank of Macon v. Macon Const. Co.* (1895) 97 Ga. 1, 25 S. E. 326 (owner of all the stock was another corporation, held, this "makes no difference in principle"); *Hopkins v. Roseclaire Lead Co.* (1874) 72 Ill. 373; *Coal &c. R. Co. v. Peabody Coal Co.* (1907) 230 Ill. 164, 82 N. E. 627; *Allemon v. Simmons* (1890) 124 Ind. 199, 23 N. E. 768; *George T. Stagg Co. v. E. H. Taylor, Jr., & Sons* (1902) 113 Ky. 709, 68 S. W. 862 (cf. *Louisville Banking Co. v. Eisenman* (1894) 94 Ky. 83, 21 S. W. 531,

VANCE v. ERIE RAILROAD CO.

1867. 32 N. J. L. 334.

ON demurrer to the declaration. Argued at June term, 1867, before the chief justice, and Justices Vredenburg, Woodhull, and Depue.

The opinion of the court was delivered by

DEPUE, J.—This action is an action of trespass on the case for malicious prosecution. To the plaintiff's declaration, the defendants have filed a general demurrer and upon the argument various grounds of demurrer were urged, all of which have been disposed of in the opinion delivered at the present term, in *Brokaw v. The New Jersey R. Co.*, 32 N. J. Law 328, except the specific objection, that an action for malicious prosecution cannot be maintained against a corporation. It is argued by counsel, that a corporation, being an ideal entity, is incapable of entertaining malice, which is an intent of the mind, and is an essential ingredient of an action for malicious prosecution.

We have seen, by the cases cited in *Brokaw v. The New Jersey Railroad and Transportation Co.*, that a corporation is liable for false and fraudulent representations, for maliciously obstructing a party in his business, for maintaining a vexatious suit, and for a malicious libel, in each of which actions an intent of the mind is quite as much involved as in an action for malicious prosecution.

1049); In the Matter of Belton (1895) 47 La. Ann. 1614, 18 So. 642; England v. Dearborn (1886) 141 Mass. 590, 6 N. E. 837; Old Dominion Copper & Co. v. Bigelow (1909) 203 Mass. 159, 89 N. E. 193; Ulmer v. Lime Rock R. Co. (1904) 98 Me. 579, 57 Atl. 1001; Rough v. Breitung (1898) 117 Mich. 48, 75 N. W. 147; Baldwin v. Canfield (1879) 26 Minn. 43, 1 N. W. 261, 276; Central Mfg. Co. v. Montgomery (1910) 144 Mo. App. 494, 129 S. W. 460; Palmer v. Ring (1906) 113 App. Div. (N. Y.) 643, 99 N. Y. S. 290; Buffalo Loan & Co. v. Medina Gas & Co. (1900) 162 N. Y. 67, 56 N. E. 505; Monongahela Bridge Co. v. Pittsburg & Co. Tract. Co. (1900) 196 Pa. St. 25, 46 Atl. 99; Rhawn v. Edge Hills Furnace Co. (1902) 201 Pa. 637, 51 Atl. 360; Commonwealth v. Monongahela Bridge Co. (1906) 216 Pa. 108, 64 Atl. 909; Parker v. Bethel Hotel Co. (1896) 96 Tenn. 252, 34 S. W. 209; Goulburn Valley Butter Fact. Co. v. Bank of New South Wales (1900) 26 Vict. L. R. 351, *Accord*.

But see *The Bellona Co. Case* (1841) 3 Bland (Md.) 442 (semble); *Swift v. Smith* (1886) 65 Md. 428, 5 Atl. 534, *Contra*.

In *Palmer v. Ring*, *supra*, the owner of substantially all the stock transferred by his individual act certain corporate property. Subsequently the receiver of the corporation demanded the property from the transferee and was refused. *Held*, [no title to the property having been acquired by the transferee, the possession thereof after refusal to surrender it became tortious, and an action of conversion properly lies.] *Miller, J.*, said: "It is well settled that the title to corporate property is in the corporate entity, and not in its stockholders (*Saranac & L. P. R. R. Co. v. Arnold*, 167 N. Y. 368; *Buffalo L. T. & S. D. Co. v. Medina Gas Co.*, 162 N. Y. 67), and, as the transfer made by *Schwickart* did not purport to be a corporate act, it was manifestly insufficient to transfer the corporate property, although he may have owned substantially all of the stock."—Eds.

In *Stevens v. Midland County Railway Co.*, 10 Exch. 352, the question whether an action for malicious prosecution would lie against a corporation was mooted in the Court of Exchequer, and Alderson, B., expressed an opinion that it would not lie, assigning as a reason, that in order to support the action, it must be shown that the defendant was actuated by a motive of the mind, and that a corporation has no mind. Platt, B., was of the opinion, that there was no evidence that the corporation had authorized the prosecution; and upon the point whether the action would lie, said: "But I do not say that a case might not arise, in which a motive might be assigned, upon which the action could be maintained." Martin, B., the only other judge who sat on the cause, concurred with Platt, B., as to the insufficiency of the evidence, and declined to give any opinion on the question, whether the action could be maintained.

In *Whitfield v. S. E. Railway Co.*, E. B. & E. 113, which was an action against a corporation for a malicious libel, the declaration was demurred to for the same reason that has been assigned here, and the opinion of Alderson, B., was cited by counsel, in support of the demurrer. The demurrer was overruled, and Lord Campbell, in delivering the opinion of the court, said, "but, considering that an action of tort or of trespass will lie against a corporation aggregate, and that an indictment may be preferred against a corporation aggregate, both for commission and omission, to be followed up by fine, although not by imprisonment, there may be great difficulty in saying that, under certain circumstances, express malice may not be imputed to, and proved against, a corporation."

In *Green v. The London Omnibus Co.*, 7 C. B. N. S. 290, which was an action for wrongfully, vexatiously, and maliciously obstructing and annoying the plaintiff in his trade, on demurrer to the declaration, it was urged that the action could not be maintained, on the same ground that malice was the *gist* of the action, and that a corporation cannot, as such, be actuated by malice. The declaration was sustained, and Erle, C. J., in delivering the opinion of the court, disposed of the argument of the counsel with the remark, that the doctrine relied on—that a corporation, having no soul, cannot be actuated by malice—is more quaint than substantial.

The same argument was addressed to the Supreme Court of the United States, in *Philadelphia, W., & B. R. Co. v. Quigley*, 21 How. 202, which was an action against a corporation for a libel, and was by that court repudiated, as a reason for exempting a corporation from liability for a libelous publication.

If actions for malicious libel—for vexatious suits, for vexatiously and maliciously obstructing another in his business, for wilful trespasses, and for assault and battery, in each of which the motives and intent of the mind are directly involved—can be maintained against a corporation aggregate, no reasons, founded on principle, can be suggested why an action for malicious prosecution should not also be sustainable against a corporation.

The reasons assigned by Erle, C. J., in *Green v. London Omnibus*

Co., for holding a corporation answerable for vexatious and malicious interference with the business of another, the extreme mischief and inconvenience which would follow from holding companies incorporated for the purpose of carrying on trade exempt from liability for intentional acts of wrong, and driving those they have injured to seek a doubtful remedy against their officers or servants, who may be wholly unable to answer the compensation which the jury may award, apply with equal force to actions for malicious prosecution.

When the nature of the action is considered, it comes strictly within the principles by which the actions above enumerated are maintainable. It must appear that the prosecution was instituted maliciously, and without probable cause. In a legal sense, any act done wilfully, to the injury of another, which is unlawful, is, as against that person, malicious and it is not necessary that the perpetrator, of such act should be influenced by ill will toward the individual, or that he entertain and pursue any bad purpose or design. *Carr v. Snelling*, 15 Pick. 337; 2 Greenl. Ev., § 453. The proof of malice need not be direct. It may be inferred by the jury, from the want of probable cause, 2 Greenl. Ev., § 453, per Lord Campbell, in *Whitfield v. S. E. Railway Co.*, and involves nothing more than a wrongful act intentionally done.

To hold a corporation amenable to this particular action, is strictly in accordance with well-settled legal principles. The wrong for which the action is the appropriate remedy, is susceptible of being committed by a corporation, by means of its agents and servants. No technical difficulties are in the way of the institution of the suit, and, at the trial, the cause can be conducted upon the established rules of evidence. To afford redress against a corporation for other intentional wrongs done by them, and deny it in this case, is an anomaly which can only be justified because of the interposition of insurmountable obstacles. No such obstacles stand in the way of the prosecution or maintenance of the action.

Under what circumstances a corporation is liable for the tortious acts of its servants or agents, even when done in obedience to the orders of its directors or officers, has been considered, in the case of *Brokaw v. The New Jersey Railroad and Transportation Co.*, *supra*. Whether, in this case, the servants or agents of the defendants, in making the arrest complained of, were acting by the authority of the corporation, is a question to be determined at the trial, in accordance with the rules stated in that case.

*Demurrer overruled.*⁴

⁴*Cornford v. Carlton Bk.* (1899) 1 Q. B. 392, (1900) 1 Q. B. 22; *Springfield & Thrashing Co. v. Green* (1886) 25 Ill. App. 106; *Hibbard v. Ryan* (1892) 46 Ill. App. 313; *Reed v. Home Savings Bk.* (1879) 130 Mass. 443; *Boogher v. Life Assn.* (1882) 75 Mo. 319; *Willard v. Holmes* (1894) 142 N. Y. 492, 37 N. E. 480; *Hussey v. Norfolk & C. Ry.* (1887) 98 N. C. 34, 3 S. E. 923 (semble), *Accord*.

Stevens v. Midland Counties Ry. (1854) 10 Ex. 352 (per Baron Alder-

WERNER v. HEARST.

1903. 177 N. Y. 63, 69 N. E. 221.

APPEAL from a judgment of the Appellate Division of the Supreme Court in the second judicial department, entered January 16, 1903, affirming a judgment in favor of plaintiff entered upon a verdict and an order denying a motion for a new trial.

GRAY, J.—The judgment appealed from must be reversed and a new trial must be had of this action; because of errors committed upon the trial, which cannot be overlooked as unimportant, or as without possible influence upon the minds of the jurors. The plaintiff sued the defendant to recover damages for personal injuries sustained by her; which are alleged to have been occasioned by the negligent conduct of the driver of a newspaper delivery wagon, employed by the defendant. She was, at the time, riding a bicycle and she alleged that the driver of the wagon carelessly drove into her and threw her down. An issue was raised, by the defendant's answer, as to his ownership of the wagon. The jury rendered a verdict in favor of the plaintiff for \$25,000 and the judgment thereupon was affirmed, unanimously, by the Appellate Division in the second department.

The injuries received by the plaintiff were of sufficient gravity, if her evidence is believed by the jurors, to justify the amount of the verdict; but this court is not concerned with questions of the amount of damages, or of the defendant's responsibility as the employer of the driver. The unanimous affirmance of the judgment on the verdict by the Appellate Division is conclusive upon us as to such questions and we are without jurisdiction to review the evidence upon the trial. All that we may do upon this appeal, which the court below has allowed to be taken to this court, is to review the exceptions taken to the rulings of the trial court upon the offers of evidence and to the instructions to the jury upon the law.

The main controversy was over the question of the defendant's relation to the driver of the wagon. The plaintiff sought by her proofs to show that he owned the wagon and employed the driver, independently of his relations to certain newspaper corporations, for whose business the wagon was used; while the defendant's proofs tended to show that he was but a stockholder and officer of a corporation to which the wagon belonged. The plaintiff was permitted, over the objection and exception of the defendant, to introduce evidence showing that the newspaper corporations had failed to file an-

son); *Abrath v. N. E. Ry.* (1886) 11 App. Cas. 247 (per Lord Bramwell), *Contra*.

See *St. Louis &c. Railroad Co. v. Dalby* (1857) 19 Ill. 352 (assault and battery); *Erie City Iron Works v. Barber* (1884) 106 Pa. St. 125; *Southern Exp. Co. v. Platten* (1899) 93 Fed. 936, 36 C. C. A. 463; *Times Pub. Co. v. Carlisle* (1899) 94 Fed. 762, 36 C. C. A. 475 (liability for exemplar, damages); *Citizen's Life Ass. Co. v. Brown* (1904) App. Cas. 423 (malicious libel).—Eds.

annual reports with the county clerk and with the state comptroller. At the request of the plaintiff, the jurors were instructed that they might consider the fact of a failure to file the reports, in deciding whether such corporations were conducted in good faith and whether their articles of association were mere forms, under which defendant had, and exercised, control. To these instructions the defendant excepted and I think that the errors in that respect, and in admitting the evidence above referred to, were important, in view of the closeness of the question of ownership, and that they were substantial, as diverting the minds of the jurors to a collateral and a false issue. The validity of the creation of the corporations and their right to exist as such, in consequence of a failure to comply with statutory conditions and requirements, as questions, had no place in such an action as this and they had no bearing upon the dispute as to the defendant's ownership and liability. We must assume that the evidence had a purpose and that it had an influence upon the jurors; for its introduction must have been with the object of invalidating the corporate status and the jurors may have been led to believe that, by reason of the failure to observe corporate obligations imposed by statute, incorporation was a sham and a device, adopted by the defendant to shield himself from liability.

The plaintiff was, thus, permitted to interject an irrelevant issue as to the character and valid existence of the corporations and it is reasonable, and, indeed, upon the record, fairly, conceivable that the jurors may have reached their verdict upon the supposition that, if the newspaper corporations were invalid, or defunct, corporate entities, the defendant was, necessarily, liable. But that is not so. They were corporations, in fact; however open to inquiry as to their right to continue as such, at the instance of the proper authorities. It was not the province of the jury to determine whether they were incorporated in good faith, or whether incorporation was a mere form and an evasive device on the defendant's part to escape an individual responsibility for the conduct of the business. (*Demarest v. Flack*, 128 N. Y. 205, 213.) The issue was whether the defendant was the employer of the negligent driver, or whether the newspaper corporation was. All evidence establishing, or tending to establish, the fact in either way was competent; but it was not competent proof upon the subject to show that the corporation had defaulted in its obligations and duties under the law, which gave it corporate rights and regulated its existence.

Other errors were committed in the rulings upon evidence and in the instructions given to the jurors, at the request of the plaintiff, bearing upon the defendant's relation to the corporations and upon their conduct, to which I think reference unnecessary; as, upon a new trial, they may not be repeated, in view of this opinion.

For these reasons, briefly stated, I think that the judgment appealed from should be reversed and that a new trial should be ordered; with costs to abide the event.

Parker, Ch. J., O'Brien, Bartlett, Martin and Cullen, JJ., concur ;
Haight, J., absent.

*Judgment reversed, etc.**

NEW YORK CENTRAL AND HUDSON RIVER RAILROAD
CO. v. UNITED STATES.

1908. 212 U. S. 481, 53 L. ed. 613, 29 Sup. Ct. 304.*

THE facts are stated in the opinion.

Mr. Justice Day delivered the opinion of the court.

This is a writ of error to the Circuit Court of the United States for the Southern District of New York, sued out by the New York Central and Hudson River Railroad Company, plaintiff in error. In the Circuit Court the railroad company and Fred. L. Pomeroy, its assistant traffic manager, were convicted for the payment of rebates to the American Sugar Refining Company and others, upon shipments of sugar from the city of New York to the city of Detroit, Michigan. The indictment was upon seven counts and was returned against the company, its general traffic manager and its assistant traffic manager. The first count, covering the offering of a rebate, was withdrawn from the jury by the district attorney, and it is unnecessary to consider it. The second count charges the making and publishing of a through tariff rate upon sugar by certain railroad companies, including the plaintiff in error, fixing the rate at twenty-three cents per 100 pounds from the New York city to Detroit, and charges the railroad company's general traffic manager and assistant traffic manager with entering into an unlawful agreement with the shippers, the American Sugar Refining Company of New York and the American Sugar Refining Company of New Jersey, and the consignees of the sugar, W. H. Edgar & Son, of Detroit, whereby it was agreed that for sugar shipped over the line, the full tariff rate being paid thereon, the railroad company should give a rebate of five cents for each 100 pounds. This count charges that during the months of April and May, 1904, shipments were made under this agreement and the regular tariff rates paid thereon. On July 14 of that year a claim for a rebate in the sum of \$1,524.99 was presented by the agents of the shipper and consignees and paid on the thirty-first day of August to Lowell M. Palmer, agent of the sugar company, for the benefit of the shippers and consignees. In each of the counts, except the sixth, the lawful rate is charged to have been 23 cents per 100 pounds. During the month of June, 1904, the same was reduced to 21 cents per 100 pounds, and the rebate agreed to and paid being 3 cents per 100 pounds. The second count

*See *Demarest v. Flack* (1891) 128 N. Y. 205, 28 N. E. 645; *Tilley v. Coykendall* (1902) 172 N. Y. 587, 65 N. E. 574.—Eds.

*Arguments and portion of opinion omitted.—Eds.

covers the shipments of April and May, 1904; the third count, the shipments for July and August, 1904; the fourth for September, 1904; the fifth for October, 1904; the sixth for June, 1904, and the seventh for April and May, 1904. In each of these counts there is an allegation of the payment of the published rate, the presentation of the claim for the rebate, and the statement of a specific sum allowed and paid on account thereof.

Upon the trial there was a conviction upon all of the six counts, two to seven inclusive. The assistant traffic manager was sentenced to pay a fine of \$1,000 upon each of the counts; the present plaintiff in error to pay a fine of \$18,000 on each count, making a fine of \$108,000 in all.

The facts are practically undisputed. They are mainly established by stipulation, or by letters passing between the traffic managers and the agent of the sugar refining companies. It was shown that the established, filed and published rate between New York and Detroit was 23 cents per 100 pounds on sugar, except during the month of June, 1904, when it was 21 cents per 100 pounds.

The sugar refining companies were engaged in selling and shipping their products in Brooklyn and Jersey City, and W. H. Edgar & Son were engaged in business in Detroit, Michigan, where they were dealers in sugar. By letters between Palmer, in charge of the traffic of the sugar refining companies and of procuring rates for the shipment of sugar, and the general and assistant traffic managers of the railroad company, it was agreed that Edgar & Son should receive a rate of 18 cents per 100 pounds from New York to Detroit.

It is unnecessary to quote from these letters, from which it is abundantly established that this concession was given to Edgar & Son to prevent them from resorting to transportation by the water route between New York and Detroit, thereby depriving the roads interested of the business, and to assist Edgar & Son in meeting the severe competition with other shippers and dealers. The shipments were made accordingly and claims of rebate made on the basis of a reduction of five cents a hundred pounds from the published rates. These claims were sent to the assistant freight traffic manager of the railroad company by Palmer, the agent of the sugar companies, and then sent to one Wilson, the general manager of the New York Central and Fast Freight Lines of Buffalo, New York. Wilson returned to the assistant traffic manager of the railroad company a cashier's draft for the amount of the claim. This draft was then sent to the agent of the sugar companies and his receipt taken. It was stipulated that these drafts were ultimately paid from the funds of the railroad company.

Numerous objections and exceptions were taken at every stage of the trial to the validity of the indictment and the proceedings thereunder. The principal attack in this court is upon the constitutional validity of certain features of the Elkins act. 32 Stat. 847. That act, among other things, provides:

"(1) That anything done or omitted to be done by a corporation

common carrier subject to the act to regulate commerce, and the acts amendatory thereof, which, if done or omitted to be done by any director or officer thereof, or any receiver, trustee, lessee, agent or person acting for or employed by such corporation, would constitute a misdemeanor under said acts, or under act, shall also be held to be a misdemeanor committed by such corporation, and upon conviction thereof it shall be subject to like penalties as are prescribed in said acts, or by this act, with reference to such persons, except as such penalties are herein changed.

* * * * *

"In construing and enforcing the provisions of this section, the act, omission or failure of any officer, agent or other person acting for or employed by any common carrier, acting within the scope of his employment, shall in every case be also deemed to be the act, omission or failure of such carrier, as well as of that person."

It is contended that these provisions of the law are unconstitutional because Congress has no authority to impute to a corporation the commission of criminal offenses, or to subject a corporation to a criminal prosecution by reason of the things charged. The argument is that to thus punish the corporation is in reality to punish the innocent stockholders, and to deprive them of their property without opportunity to be heard, consequently without due process of law. And it is further contended that these provisions of the statute deprive the corporation of the presumption of innocence, a presumption which is part of due process in criminal prosecutions. It is urged that as there is no authority shown by the board of directors or the stockholders for the criminal acts of the agents of the company, in contracting for and giving rebates, they could not be lawfully charged against the corporation. As no action of the board of directors could legally authorize a crime, and as indeed the stockholders could not do so, the arguments come to this: that owing to the nature and character of its organization and the extent of its power and authority, a corporation cannot commit a crime of the nature charged in this case.

Some of the earlier writers on common law held the law to be that a corporation could not commit a crime. It is said to have been held by Lord Chief Justice Holt (Anonymous, 12 Modern, 559) that "a corporation is not indictable, although the particular members of it are." In Blackstone's Commentaries, chapter 18, § 12, we find it stated: "A corporation cannot commit treason, or felony, or other crime in its corporate capacity though its members may in their distinct individual capacities."

The modern authority, universally, so far as we know, is the other way. In considering the subject, Bishop's New Criminal Law, § 417, devotes a chapter to the capacity of corporations to commit crime, and states the law to be: "Since a corporation acts by its officers and agents their purposes, motives, and intent are just as much those of the corporation as are the things done. If, for example, the invisible, intangible essence of air, which we term a

corporation, can level mountains, fill up valleys, lay down iron tracks, and run railroad cars on them, it can intend to do it, and can act therein as well viciously as virtuously." Without citing the state cases holding the same view, we may note *Telegram Newspaper Company v. Commonwealth*, 172 Massachusetts, 294, in which it was held that a corporation was subject to punishment for criminal contempt, and the court, speaking by Mr. Chief Justice Field, said: "We think that a corporation may be liable criminally for certain offenses of which a specific intent may be a necessary element. There is no more difficulty in imputing to a corporation a specific intent in criminal proceedings than in civil. A corporation cannot be arrested and imprisoned in either civil or criminal proceedings, but its property may be taken either as compensation for a private wrong or as punishment for a public wrong." It is held in England that corporations may be criminally prosecuted for acts of misfeasance as well as nonfeasance. *Queen v. Great North of England Railway Company*, 9 Queen's Bench, 315.

It is now well established that in actions for tort the corporation may be held responsible for damages for the acts of its agent within the scope of his employment. *Lake Shore & Michigan Southern R. v. Prentice*, 147 U. S. 101, 109, 111.

And this is the rule when the act is done by the agent in the course of his employment, although done wantonly or recklessly or against the express orders of the principal. In such cases the liability is not imputed because the principal actually participates in the malice or fraud, but because the act is done for the benefit of the principal, while the agent is acting within the scope of his employment in the business of the principal, and justice requires that the latter shall be held responsible for damages to the individual who has suffered by such conduct. *Lothrop v. Adams*, 133 Massachusetts, 471.

A corporation is held responsible for acts not within the agent's corporate powers strictly construed, but which the agent has assumed to perform for the corporation when employing the corporate powers actually authorized, and in such cases there need be no written authority under seal or vote of the corporation in order to constitute the agency or to authorize the act. *Washington Gas-light Co. v. Lansden*, 172 U. S. 534, 544.

In this case we are to consider the criminal responsibility of a corporation for an act done while an authorized agent of the company is exercising the authority conferred upon him. It was admitted by the defendant at the trial that at the time mentioned in the indictment the general freight traffic manager and the assistant freight traffic manager were authorized to establish rates at which freight should be carried over the line of New York Central and Hudson River Company, and were authorized to unite with other companies in the establishing, filing and publishing of through rates, including the through rate or rates between New York and Detroit referred to in the indictment. Thus the subject-matter of

making and fixing rates was within the scope of the authority and employment of the agents of the company, whose acts in this connection are sought to be charged upon the company. Thus clothed with authority, the agents were bound to respect the regulation of interstate commerce enacted by Congress, requiring the filing and publication of rates and punishing departures therefrom. Applying the principle governing civil liability, we go only a step farther in holding that the act of the agent, while exercising the authority delegated to him to make rates for transportation, may be controlled, in the interest of public policy, by imputing his act to his employer and imposing penalties upon the corporation for which he is acting in the premises.

It is true that there are some crimes, which in their nature cannot be committed by corporations. But there is a large class of offenses, of which rebating under the Federal statutes is one, wherein the crime consists in purposely doing the things prohibited by statute. In that class of crimes we see no good reason why corporations may not be held responsible for and charged with the knowledge and purposes of their agents, acting within the authority conferred upon them. 2 Morawetz on Corporations, 733; Green's Brice on Ultra Vires, 366. If it were not so, many offenses might go unpunished and acts be committed in violation of law, where, as in the present case, the statute requires all persons, corporate or private, to refrain from certain practices forbidden in the interest of public policy.

It is a part of the public history of the times that statutes against rebates could not be effectually enforced so long as individuals only were subject to punishment for violation of the law, when the giving of rebates or concessions enured to the benefit of the corporations of which the individuals were but the instruments. This situation, developed in more than one report of the Interstate Commerce Commission, was no doubt influential in bringing about the enactment of the Elkins Law, making corporations criminally liable.

This statute does not embrace things impossible to be done by a corporation; its objects are to prevent favoritism, and to secure equal rights to all in interstate transportation, and one legal rate, to be published and posted and accessible to all alike. *New Haven Railroad Company v. Interstate Commerce Commission*, 200 U. S. 399; *Armour Packing Co. v. United States*, 209 U. S. 56.

We see no valid objection in law, and every reason in public policy, why the corporation which profits by the transaction, and can only act through its agents and officers, shall be held punishable by fine because of the knowledge and intent of its agents to whom it has intrusted authority to act in the subject-matter of making and fixing rates of transportation, and whose knowledge and purposes may well be attributed to the corporation for which the agents act. While the law should have regard to the rights of all, and to those of corporations no less than to those of individuals, it cannot shut its eyes to the fact that the great majority of business

transactions in modern times are conducted through these bodies, and particularly that interstate commerce is almost entirely in their hands, and to give them immunity from all punishment because of the old and exploded doctrine that a corporation cannot commit a crime would virtually take away the only means of effectually controlling the subject-matter and correcting the abuses aimed at.

There can be no question of the power of Congress to regulate interstate commerce, to prevent favoritism and to secure equal rights to all engaged in interstate trade. It would be a distinct step backward to hold that Congress cannot control those who are conducting this interstate commerce by holding them responsible for the intent and purposes of the agents to whom they have delegated the power to act in the premises.

It is contended that the Elkins Law is unconstitutional, in that it applies to individual carriers as well as those of a corporate character, and attributes the act of the agent to all common carriers, thereby making the crime of one person that of another, thus depriving the latter of due process of law and of the presumption of innocence which the law raises in his favor. This contention rests upon the last paragraph of § 1 of the Elkins Act, which is as follows, 32 Stat. 847:

"In construing and enforcing the provisions of this section the act, omission, or failure of any officer, agent, or other person acting for or employed by any common carrier acting within the scope of his employment shall in every case be also deemed to be the act, omission, or failure of such carrier as well as that of the person."

We think the answer to this proposition is obvious; the plaintiff in error is a corporation, and the provision as to its responsibility for acts of its agents is specifically stated in the first paragraph of the section. There is no individual in this case complaining of the unconstitutionality of the act, if objectionable on that ground, and the case does not come within that class of cases in which unconstitutional provisions are so interblended with valid ones that the whole act must fall, notwithstanding its constitutionality is challenged by one who might be legally brought within its provisions. *Employers' Liability Cases*, 207 U. S. 463. It may be doubted whether there are any individual carriers engaged in interstate commerce, and every act is to be construed so as to maintain its constitutionality if possible. There can be no question that Congress would have applied these provisions to corporation carriers, whether individuals were included or not. In this view the act is valid as to corporations. *Berea College v. Kentucky*, 211 U. S. 45, 55.

It is contended that the court should have sustained the objection to the indictment upon the ground that the corporation and its agent could not be legally joined therein, but we think a fair construction of the act permits both the corporation and the agent to be joined in one indictment for the commission of the offense. The

purpose of the act was to make the act one of the corporation as well as of the agent, and to include both within the prohibitions and restrictions of the statute, and this seems to be the accepted practice. Thompson on Corporations 4495.

* * * * *
We have noted all the assignments of errors which involve questions of a substantial character.

We find no error in the proceedings of the Circuit Court, and its judgment is

*Affirmed.*⁷

UNITED STATES v. NEW YORK HERALD CO.

1907. 159 Fed. 296.

AT LAW. On demurrer to the indictment of defendant corporation under Rev. Stat. § 3893, as amended (U. S. Comp. St. 1901 p. 2658).

HOUGH, District Judge. I. As to the capacity of a corporation to commit the crime alleged in this indictment, I see no reason to depart from United States v. MacAndrews & Forbes Company (C. C.) 149 Fed. 823.⁸

⁷United States v. Alaska Packers' Ass'n. (1901) 1 Alaska 217 (taking salmon unlawfully); Southern Ry. Co. v. State (1906) 125 Ga. 287, 54 S. E. 160 (failure to supply drinking water on trains); Southern Express Co. v. State (1907) 1 Ga. A. 700, 58 S. E. 67 (selling liquor illegally to minors); Franklin Union No. 4 v. People (1906) 220 Ill. 355, 77 N. E. 176 (contempt); State v. Baltimore & C. R. Co. (1889) 120 Ind. 298, 22 N. E. 307 (obstructing highway); Telegram Newspaper Co. v. Commonwealth (1899) 172 Mass. 294, 52 N. E. 445 (criminal contempt); State v. Morris & C. R. Co. (1852) 23 N. J. L. 360 (criminal nuisance); State v. Passaic Co. Agr. Society (1892) 54 N. J. L. 260, 23 Atl. 680 (keeping a disorderly house); People v. Woodbury Dermatological Inst. (1908) 192 N. Y. 454, 85 N. E. 697 (unlawfully advertising to practice medicine); State v. First Nat. Bk. (1892) 2 S. Dak. 568, 51 N. W. 587 (usury); State v. Atchison & C. Pub. Co. (1879) 3 Lea [Tenn.] 729 (libel); State v. Baltimore & C. R. Co. (1879) 15 W. Va. 362 (Sabbath breaking); United States v. Kelso (1898) 86 Fed. 304 (violating Eight-Hour Law); United States v. Van Schaick (1905) 134 Fed. 592 (manslaughter, the result of lack of life preservers on the steamboat "General Slocum"), *Accord*.

See the general review of authorities in Queen v. Great North. Ry. Co. (1846) 9 Q. B. 316.

In People v. Rochester & C. Light Co. (1909) 195 N. Y. 102, 88 N. E. 22, the Court stated that "a definition of certain forms of manslaughter might be formulated which would be applicable to a corporation." (p. 107). Under Penal Code, sec. 179, however, defining homicide as "the killing of one human being by the act, procurement or omission of another," meaning another human being, *held*, a corporation could not be guilty.—Eds.

⁸Indictment of corporations under the "Sherman Anti-Trust Law." On demurrer, *held*, a corporation may be liable criminally for the offense of conspiracy. Hough, J., remarked: "It seems to me as easy and logical to ascribe to a corporation an evil mind as it is to impute to it a sense of contractual obligation."—Eds.

2. Under Rev. St. 3893, as amended [U. S. Comp. St. 1901, p. 2658], the indictment alleges that the corporation defendant "did knowingly deposit and cause to be deposited" in the United States mail certain unmailable matter, and that when such deposit was made the corporation "well knew the contents of the same." The question presented on demurrer is not whether the corporation did as matter of fact "knowingly" deposit the publication in the mail, or as matter of fact, "well know" the contents of the same, but whether it can knowingly deposit, and well know the contents of, an obscene newspaper. Reading the act under which this indictment is brought in conjunction with the statutory construction law (Rev. St. U. S. § 1 [U. S. Comp. St. 1901, p. 3]), and observing that the act in question was passed subsequent to February 25, 1871, I have no doubt that it was the intention of Congress to make section 3893 applicable to corporations.

Taking as the measure of the knowledge required in cases like this the decisions in *Rosen v. U. S.*, 161 U. S. 29, 16 Sup. Ct. 434, 40 L. ed. 606, and *Dunlop v. United States*, 165 U. S. 486, 17 Sup. Ct. 375, 41 L. ed. 799, it is not to be doubted that, if by corporate act (e. g., a vote of the board of directors) the obnoxious publication was directed to be placed in the mail, knowledge of its contents and knowledge of the character thereof would be chargeable against the corporation, even though there was a consensus of opinion on the part of the directors that the paper was not of the forbidden character (the *Rosen Case*); it being enough that said directors in their official capacity were aware of the insertion in the newspaper of matter obnoxious (in the opinion of court and jury) to the statute (the *Dunlop Case*). To fasten this species of knowledge upon a corporation requires no other or different kind of legal inference than has long been used to justify punitive damages in cases of tort against an incorporated defendant. If a corporation can corporately know that an engineer is a habitual drunkard (*Cleghorn v. N. Y. Central, etc., R. R. Co.*, 56 N. Y. 44, 15 Am. Rep. 375), it can even more surely know the ordinary contents of a newspaper the publication of which is its sole reason for existence.

Of course, the capacity for knowledge and the fact of knowledge are quite different things. The first is a question of law, and must decide this demurrer. The second is a mixed question of law and fact, and, as applied to this case, its answer will depend upon the authority and corporate importance of the human beings responsible to the corporation for the reception, publication, and mailing of the advertisements here complained of as unmailable under the statute.

*Let the demurrer be overruled.**

* *Cf. State v. White* (1902) 96 Mo. App. 34, 69 S. W. 684.—Eds.

MONTGOMERY WEB CO. v. DIENELT.

1890. 133 Pa. St. 585, 19 Atl. 428.¹⁰

BEFORE Paxson, C. J., Sterrett, Green, Clark, Williams, McCollum and Mitchell, JJ.

On March 8, 1886, on application of the sheriff of Montgomery county, setting forth that certain chattels, levied on as the property of the Aronia Fabric Company, at the suit of Herman Dienelt and George F. Eisenhardt, trading as Dienelt & Eisenhardt, had been claimed by the Montgomery Web Company, the court granted a rule for an interpleader under the act of April 10, 1848, P. L. 450. The rule was made absolute the same day, and subsequently an issue, in which the Montgomery Web Co. was plaintiff, and Dienelt & Eisenhardt, defendants, was framed to determine the claim of title made by the Montgomery Web Company.

At the trial on October 9, 1888, the plaintiff in the issue, the Montgomery Web Co., called Herman Hamburger, who, being shown a paper purporting to be a bill of sale from the Aronia Fabric Co. to the plaintiff of certain chattels a part of which were admittedly the property in dispute, in consideration of one dollar and the assumption by the assignee of certain specified debts of the assignor, testified to the execution of the paper by the officers of the Aronia Fabric Co., including himself as its president, identified the corporate seal of that company affixed thereto, and stated that the property described in the bill of sale was purchased from said company by the plaintiff company, and was delivered to the latter.

On cross-examination, the witness testified that at the time the bill of sale was made he was president of each of the companies above named; that there was then pending a suit against the Aronia Fabric Co., brought by Dienelt & Eisenhardt, who afterwards recovered therein the judgment for the collection of which the goods in controversy were levied on; that the witness did not attend the trial of that case, and it went by default; that the goods transferred by the bill of sale embraced all the property of the Aronia Fabric Co., except certain looms, which were left at the mill it had operated for the purpose of paying rent and any little claims there might be against them, and the agent of the landlord was so notified; that those looms were afterwards sold on landlord's warrant, as the witness understood, for less than the amount of the rent; that the Montgomery Web Co. was a corporation composed entirely of old stockholders and creditors of the Aronia Fabric Co., embracing all unpaid creditors of the latter except Dienelt & Eisenhardt; that the stockholders in the old company paid no cash for their stock in the new one, but the property was turned over to the new company under an arrangement by which those stockholders received stock in it, equal in amount to their holdings of stock in the old company,

¹⁰ Statement abridged; arguments omitted.—Eds.

and the Montgomery Web Co. paid the claims of all the creditors, other than Dienelt & Eisenhardt, partly in cash and partly in its stock; that no notice of the intention to carry out this arrangement was given to Dienelt & Eisenhardt, because it was supposed the company had a just defense to their claim; that Dienelt & Eisenhardt, having learned of it in some way unknown to the witness, endeavored to prevent the removal of the property by means of an attachment under the fraudulent debtor's act of 1869, but the court dissolved their attachment. Being shown a paper, purporting to be an affidavit made by himself, in connection with the proceedings upon the attachment spoken of, and containing the statement that by the terms of the transfer all the debts of the Aronia Fabric Co. were to be paid by the Montgomery Web Co., the witness identified his signature to the affidavit, but denied that he intended to swear to this statement as to Dienelt & Eisenhardt, who "were excepted all the way through." He testified, further, that the amount of stock of the Montgomery Web Co. that was given to the stockholders of the Aronia Fabric Co., was considerably more than half of the entire number of shares.

The verdict of the jury was in favor of the plaintiff and the defendants appealed.

OPINION, MR. JUSTICE MITCHELL:

Two questions are presented in this case: First, whether the transfer from the Aronia company to plaintiff was fraudulent in fact, as against the appellants; and, secondly, whether it was fraudulent in law.

On the first question, the verdict of the jury was in favor of the good faith of the transaction; but unfortunately it is without weight, as it was rendered under a charge which scarcely permitted any other result, and which was justly open to the exceptions taken to it. Fraud, as has so often been said, can rarely be proved by direct and positive testimony, and great liberality is always allowed in the introduction of evidence having a tendency to show it. "When creditors are about to be cheated," says Chief Justice Black in *Kaine v. Weigley*, 22 Pa. 183, "it is very uncommon for the perpetrators to proclaim their purpose, and call in witnesses to see it done. A resort to presumptive evidence, therefore, becomes absolutely necessary, to protect the rights of honest men from this as from other invasions." The present case followed the usual course. Defendants had to get their testimony from the other side, and from the circumstances, and were not able to make positive and direct proof of the fraudulent intent, but had to rely upon circumstances pointing thereto. In his charge, the learned judge took these up seriatim, and disposed of them summarily in the passages assigned for error, as follows: "What facts are before you to show that there was any fraud in this transaction? The mere fact that they (appellants) were not provided for would not in itself be fraud. Now, it appears that a paper was drawn up and signed by all the creditors except these particular parties. This was a per-

fectly legal transaction. If this transferring was not done for the purpose of defrauding these particular creditors, it was perfectly proper." And again: "Now, the facts and circumstances related here to show fraud are, first, that they (defendants) were not thus provided for; and, in the second place, certain declarations made by the president . . . in an affidavit. . . . (The jury) must determine from the facts before them, and from all the inferences to be drawn from these facts. Because defendants may lose their claim, is not evidence that they were intended to be defrauded." This was not an adequate presentation of the case. It omits all mention of the facts that the failure to provide for defendants, to include them in the paper, or to give them notice of the proceeding, was intentional, always a cardinal point in the proof of fraud; and it makes no reference to the removal of the Aronia company's goods without leaving enough to pay even the rent, to the fact that the transfer was made on the eve of a trial which was sure to result in a judgment in favor of appellants, and perhaps to other circumstances of suspicion. But the substantial defect of the charge is in its treatment of the items of evidence, one by one, without at any time directing the view of the jury to their united force. There probably never was a case of circumstantial evidence that could not be blown to the winds by taking up each item separately, and dismissing it with the conclusion that it does not prove the case. The cumulative force of many separate matters, each perhaps slight, as in the familiar bundle of twigs, constitutes the strength of circumstantial proof. This presentation of the case to the jury we unfortunately do not find anywhere, and, for want of it, we are obliged to sustain the third, fourth, and fifth assignments of error.

But, secondly, was this transfer fraudulent in law? Here again, the true point of the case has been unfortunately overlooked. The question is stated in the opinion of the court to be whether a corporation can lawfully dispose of its assets without the assent of all its creditors, there being no actual fraud intended; and this is the question that has been argued here by appellee. But it is only half the question, and the pinch of the case lies in the omitted portion: Can the stockholders of a corporation make such a transfer to *themselves*? The Montgomery company is substantially the Aronia company under a new name. More than half its stock is held by the old stockholders by virtue of their ownership of the old stock, without any other consideration. On the view of the question that appellees assume to be contended for, they have argued that the same law as to the use of its assets to pay its debts should be applied to a corporation as to an individual, even to the extent of sanctioning preferences, and this might be conceded without really touching the case. But the illustration, if appropriate, is fatal to the appellee; for, in the case of an individual, a transfer to his wife or his agent, or anybody who should merely represent himself under another name, would be unquestionably void against creditors. The only real difficulty in the present case is whether the stockholders are

so completely severed, in the view of the law, from the corporation behind which they hide, as to prevent a creditor from asserting their identity in fact, for the purpose of securing payment out of property which was theirs under one name, and is still theirs under another. Is the Montgomery company so completely a new and different person from the Aronia company that the law must close its eyes to the fact that the difference is a mere juggle of names? We do not think there is any compulsion to such legal blindness. Settled general principles, and the analogies of the law, are against such a contention. If the corporation had merely changed its name, there could have been no doubt of the continued liability of the property. As already said, a majority of the stockholders in the new company are simply the stockholders of the old company holding as such, and without other consideration. As to these, it has been a mere change of name. As to the other or new stockholders, it appears from the agreed facts that they were creditors of the old company, and hold their present stock solely in consideration of their former claims as creditors. They paid nothing else for it; and they must have known that the new corporation into which they entered in this way was not a new enterprise in the regular course of business under the incorporation act of 1874 as it professed to be, but a new turn in the old enterprise, all of whose property was being practically handed over, not to them alone in payment, which they might, perhaps, rightfully have accepted, but to them in conjunction with their late debtors. Under such circumstances, they were bound to take notice of the nature of the transaction, and to know that equity would still regard the property as a trust for the payment of existing debts, and would follow it on behalf of creditors until it should get into the hands of innocent purchasers for value. Such purchasers they were not. The old stockholders were not purchasers for value at all; and the new stockholders were not innocent, for they know, or were bound to take notice, of the taint in their co-adventurers' title. We are of opinion that, as to the stockholders in the Aronia company, this was a transfer of property by a debtor with the retention of an interest in himself, within the settled rule of law that makes such transfers void against creditors, and that, as to the Aronia creditors who became new stockholders in the Montgomery company, they took with such notice as prevents them from claiming now as innocent holders for value against the appellants as execution creditors of the old corporation. It is not worth while to cite authorities for these principles. They are settled and familiar. The only question that can be made is upon their application; and the novelty in this, if there be any, is simply the novelty of circumstances. The only case of similar facts that has been found is *Hibernia Ins. Co. v. Transportation Co.*, 13 Fed. 516; and in that the Circuit Court of the United States reaches a similar conclusion. "This court holds," says McCrary, C. J., "that the sale by the Babbage company of all its property to another corporation, composed mostly, if not wholly, of the same persons, was

fraudulent and void as to all creditors of the former company not assenting thereto. . . . The fair inference from the transaction is that the old company was about to be dissolved, and to cease to be. It was to be absorbed by the new company. This is the inevitable consequence of the formation of the new company, composed substantially of the same persons, to transact the same business, at the same places, and with the same property. By the transfer, the creditors of the old company were deprived of the means of enforcing their claims. . . . Equity will not compel the creditor of a corporation to waive his right to enforce his claim against the visible and tangible property of the corporation, and to run the chances of following and recovering the value of shares of stock after they are placed on the market." And Treat, D. J., added: "A corporation . . . cannot change its name, or assume the form of a new corporation, and thus escape its obligations." The court drew a distinction between an individual and a corporation, as to parting with all its assets even for the payment of bona fide debts, and not only held the transfer void even irrespective of the identity of the stockholders, but held the new corporation liable to the creditors of the old to the extent of the assets so received. It is not necessary for us to go so far. We only hold that, under the circumstances, specific property of the old corporation may be followed, as in other cases of transfers fraudulent as to creditors.

It is said in appellee's argument that the whole of the property of the Aronia company was not sold. But, in fact, the portion left was not enough to pay the landlord's preferred claim for rent; and, as to this creditor the transfer was of all the available assets, and left him nothing within reach for payment of his claim.

*Judgment reversed, and now judgment for defendant on the point reserved.*¹¹

HIGGINS v. CALIFORNIA PETROLEUM &c. CO., ET AL.

1905. 147 Cal. 363, 81 Pac. 1070.

APPEAL from a judgment of the Superior Court of Santa Barbara County. D. K. Trask, Judge presiding.

The facts are stated in the opinion of the court.

¹¹ Kellogg v. Douglas County Bank (1897) 58 Kan. 43, 48 Pac. 587; Bremen Savings Bk. v. Branch &c. Saw Co. (1891) 104 Mo. 425, 16 S. W. 209; Lusk v. Riggs (1902) 65 Neb. 258, 91 N. W. 243; Terhune v. Hackensack Savings Bk. (1889) 45 N. J. Eq. 344, 19 Atl. 377; Booth v. Bunce (1865) 33 N. Y. 139; First National Bank v. Trebein Co. (1898) 59 Ohio St. 316, 52 N. E. 834; Andres v. Morgan (1900) 62 Ohio St. 236, 56 N. E. 875; Bennett v. Minott (1896) 28 Ore. 339, 39 Pac. 997, 44 Pac. 288; Vance v. McNabb Coal &c. Co. (1892) 92 Tenn. 47, 26 S. W. 424; Hibernia Ins. Co. v. St. Louis &c. Transp. Co. (1882) 13 Fed. 516, *Accord*.

See article "Piercing the Veil of Corporate Entity" by I. Maurice Wormser, 12 Columbia Law Rev. 496, 498-502 (June, 1912).—Eds.

McFARLAND, J.—Each of the three defendants called the “California Petroleum and Asphalt Company,” the “Alcatraz Asphalt Company,” and the “Alcatraz Company,” is a corporation; and this action is brought by plaintiff, as one of the lessors in a certain lease of asphalt mines, to recover from said defendants certain rents, or royalties, reserved in the lease. The trial court rendered judgment for a certain sum of money which is found to be due as such royalties, and from the judgment the said defendants appeal, bringing up rulings and evidence in a bill of exceptions.

Most of the main questions in the case were settled on two former appeals arising out of this same lease. In one of them,—namely, *Higgins v. California Petroleum and Asphalt Co.*, 109 Cal. 304, 41 Pac. 1087, the present plaintiff, Higgins, was plaintiff, and the defendant herein first above named, the California Petroleum and Asphalt Company, was defendant; and in the other case,—namely, *Higgins v. California Petroleum and Asphalt Co. and Alcatraz Asphalt Co.*, 122 Cal. 373, 55 Pac. 155,—Higgins was plaintiff, and the two corporations first named in the complaint herein—to wit, the California Petroleum and Asphalt Company and the Alcatraz Asphalt Company—were defendants. In those two cases many of the facts pertinent to the present case are stated, and also the principles of law involved; and this present opinion will consist largely of references to those cases and quotations from the opinions therein.

On June 4, 1887, the plaintiff herein, Higgins, and Mary A. Ashley were each the owner in severalty of a tract of land, each tract lying alongside of and adjoining the other. Running horizontally and continuously through both of these tracts there was a deposit of bituminous rock. On said June 4, 1887, the plaintiff herein and said Ashley jointly executed a written lease to one Joseph Scheerer for the term of twenty years of all the bituminous rock lying in said two tracts of land; and the lessee covenanted, among other things, to pay to the lessors on the first day of every month during the term “the sum of fifty cents per ton for each and every gross ton of bituminous rock and liquid asphaltum which he may have mined, taken or removed from said premises during the calendar month then next preceding.” In December, 1891, the defendant and appellant herein, the California Petroleum and Asphaltum Company (hereinafter called, for brevity, the C. P. and A. Co.), became the sole owner of said lease by assignment; and in June, 1902, the said Mrs. Ashley conveyed to said C. P. and A. Co. all that part of the land described in the lease which she severally owned. For several months after said conveyance by Mrs. Ashley the C. P. and A. Co. paid to the plaintiff herein one-half of the stipulated rent or royalty (twenty-five cents per ton). Mrs. Ashley treating her interest in the lease as extinguished or merged in the said deed of her land. But differences arose between plaintiff herein and the C. P. and A. Co., and the latter, after April 1, 1893, refused to make further payments of royalty or rent. Thereupon the plaintiff herein,

Higgins, commenced the action of Higgins v. California Petroleum and Asphalt Co., which was reported in 109 Cal., as above stated. The object of that action was to recover one thousand dollars unpaid royalty on four thousand tons of rock at twenty-five cents per ton, alleged to have been mined from the deposit during the months of April, May, June, and July, 1893. The court found that the royalties of the defendant amounted to \$671.25, and rendered judgment for plaintiff for that amount. The C. P. and A. Co. appealed, and the judgment and order denying defendant's motion for a new trial were by this court affirmed. (109 Cal. 304, 41 Pac. 1087.) In that case this court declares that the lease, although made jointly by different owners of contiguous properties, was a valid lease. The court said, through its commissioner, as follows: "Had the lessors in this case been tenants in common of the demised premises, the effects of a conveyance by Ashley of her reversionary estate therein to the lessee would have been to merge her interest in the leasehold term in the reversion, and to extinguish *pro tanto* the covenant of the lessee to pay rent; yet, thereafter, Higgins would have been entitled to receive from the lessee the same proportion of rent as before such conveyance (citing authorities); and I perceive no reason why the effects of Ashley's conveyance of her separate part of the demised premises, of which she was sole owner, should not be substantially the same as they would have been if the lessors had been tenants in common of every part of such premises; the only possible difference being in the mode of apportioning the rent. Had they been tenants in common, Higgins would still be entitled to a part of the rent proportionate to his undivided portion of the demised premises, but as they are not tenants in common he is entitled, in the absence of an express or presumed agreement to the contrary, to a portion of the royalty proportionate to the comparative value of his distinct part of the demised premises; and in this case the terms of the lease warrant the presumption that each lessor was to receive one-half of the royalty, and such presumption is in perfect accord with the practical construction of the lease by the parties thereto, up to April, 1893.

"The fact that, prior to the commencement of this action, the lessee had elected to mine only in that part of the 'deposit' lying within the Ashley tract detracts nothing from the rights of Higgins to demand his proper share of the royalty, nor from the obligation of defendant to pay it. The royalty of fifty cents on each ton of rock mined was, by the terms of the lease, to be paid to the lessors, not to the individual lessor from whose land the rock may have been mined. The lease does not restrict the mining to any particular part of the deposit at any time. The lessee has had the right, at all times since the execution of the lease, to mine any part of the deposit, and will continue to have such right until the expiration of the term of twenty years, only about five years of which had elapsed when this action was commenced, and more than one-half of the term is still in the future, during which defendant is at liberty to

mine exclusively in that part of the deposit lying within the Higgins tract, and may completely exhaust it. The royalty per ton of rock mined is but a mode of estimating the rent to be paid for the right to occupy exclusively the whole premises demised, and to mine any part or all parts thereof at any time during the term, at the election of the lessee."

After the decision of the case last above referred to, the C. P. and A. Co. conveyed the land which had been conveyed to it by Mrs. Ashley to a new corporation called the Alcatraz Asphalt Company, but did not assign to the latter the said lease. After this, rock was taken out of the deposit as before, and apparently under the same management—the rock, however, being taken out only from that part of the leased land which had been owned by Mrs. Ashley and conveyed by her to the C. P. and A. Co. The new corporation claimed that it was taking out the rock, and that, as it was not an assignee of the lease, it was not liable to Higgins for any part of the royalty, and refused to pay him any royalty or rent. Thereupon Higgins brought another action to recover from the two companies for royalties due, and recovered judgment; and from this judgment both companies appealed. The appeal in that case is the one reported in 122 Cal., above referred to. The court in that case affirmed the judgment upon the ground that the two corporations were substantially the same, and that the lease could not be avoided by the scheme of a new corporation organized by the incorporators of the old one.

The court said: "But the court below found in substance that the California Petroleum and Asphalt Company and the Alcatraz Asphalt Company (its alleged grantee) are identical, and that the mining operations conducted by the latter company on this land were in reality conducted by the former company. On this ground, the respondent contends that both companies are liable for the royalties in question.

"We think that there was evidence to sustain this finding. It shows that the new company was substantially a reorganization of the old one. In the old company there was only one real stockholder, and all of the stock issued by the new company was issued to him, the sole consideration being a debt which the old company owed him. It is true that shortly afterward he transferred some of his stock to some Eastern capitalists, and had this in view when the new company was formed. But we cannot agree with appellant that this fact affects the case." And the court further said: "The evidence, moreover, strongly suggests, if it does not establish, that the main, and perhaps the sole, purpose of this organization was to evade the obligations of the lease. While transferring to the new company its land and all of the business and assets, it retained the lease. While transferring to the new company its land and all of the business and assets, it retained the lease, which could be of no avail in its hands. It is a legitimate inference that this was done purposely, and, if so, the only possible object would be to prevent

Higgins from collecting royalties. The old company was to continue to be the lessee, but was to do no mining; while it was to permit the new company, its *alter ego*, to mine without any responsibility therefor. We therefore think that the court below was justified in holding that the new company was only the old one under another name; and that being so, it is plain that their responsibility to Higgins was not impaired by this merely nominal transfer. (Citing cases.) It is true that the court did not find that there was any actual fraud in the transaction; but we think that such a transfer as against the holder of an existing obligation is constructively fraudulent as a matter of law."

After the latter decision, a third corporation was formed under the laws of West Virginia,—to wit, the defendant herein, the Alcatraz Company; and to this third corporation the said land formerly owned by Mrs. Ashley was conveyed by the second-named corporation and defendant, the Alcatraz Asphalt Company. After this, rock was taken out as before, and this action is brought to recover royalties therefor. The court found that a certain number of tons of rock were taken out, and that twenty-five cents per ton amounted to a certain sum, for which judgment was rendered for plaintiff. The findings as to the amount of rock taken out and not paid for, and the amount due for the royalties, are supported by the evidence, and, indeed, are not assailed. The contention is,—substantially as in the former cases,—that the defendants are not liable because the last-named corporation conducted the business, and not being bound by the lease, etc., is not under any obligation to pay royalties to the lessor, Higgins.

However, we take the decisions of this court in the two cases above referred to as declaring the law applicable to those two cases; and we cannot see any substantial difference between the second of those cases and the case at bar. In the present case the court found that the three corporations defendant are really the same; that the Alcatraz Asphalt Company was organized by the officers and stockholders of the C. P. and A. Co., and the Alcatraz Company was organized by the stockholders of the Alcatraz Asphalt Company; that all three corporations "had their offices together in the same room, had practically the same officers and were organized by the same persons and for substantially the same purposes." And it further found "that the operations conducted on the leased premises during the time covered by the amended complaint in this action, under the name of Alcatraz Company, were in reality conducted by or under the authority of the Alcatraz Asphalt Company and the California Petroleum and Asphalt Company." Appellants contend that these findings are not warranted by the evidence; but we think that they are. The evidence in the case at bar as clearly shows the relation as found by the court of the third corporation to the two former ones as the evidence in the case reported in 122 Cal. shows the relation of the second corporation, the Alcatraz Asphalt Company, to the first corporation, the C. P. and A. Co. * * *

We are satisfied that the points here made for a reversal are covered, substantially, by the two former decisions against the contentions of the appellants.

The judgment appealed from is affirmed.

LORIGAN, J., and HENSHAW, J., concurred.¹²

DONOVAN v. PURTELL.

1905. 216 Ill. 629, 75 N. E. 334.¹³

APPEAL from the Appellate Court for the Fourth District; heard in that court on appeal from the Circuit Court of St. Clair county; the HON. R. D. W. HOLDER, Judge, presiding.

This is an action in assumpsit, begun by appellee against appellant on November 24, 1903, by attachment in the circuit court of St. Clair county. The writ of attachment was levied on appellant's interest in certain land situated in that county. Before the trial, to-wit, on March 23, 1904, by agreement of the parties an order was entered, releasing the real estate, levied upon under the writ of attachment, upon the execution and filing by appellant of an indemnity bond. The declaration consists of the common counts for money lent by appellee to defendant at his request; for money paid out and expended by appellee for the use of appellant at his request; for money received by appellant for the use of appellee; for money for interest on divers sums of money forborne by appellee to appellant at his request, etc. A bill of particulars was filed, which, besides the items for money loaned and due in 1901, contains items for money lent by appellee to appellant in the name of the Fidelity Realty Company in 1901, and for money lent to appellant by appellee and promised to be paid by him in the name of the J. T. Donovan Real Estate Company in 1901. The general issue was filed to the declaration. A trial was had before the court and jury, resulting in a verdict in favor of appellee against appellant for the sum of \$1,430.00, from which the plaintiff remitted the sum of \$71.80, making the amount of the verdict \$1,358.20, which *remittitur* was approved by the court. Motion for new trial was overruled and judgment rendered on the verdict in favor of appellee against appellant for \$1,358.20 and costs. An appeal was taken to the Appellate Court where the judgment has been affirmed. The present appeal is prosecuted from such judgment of affirmance.

¹² In *Miller & Lux v. East Side Canal &c. Co.* (1908) 211 U. S. 293, 53 L. ed. 189, *held*, that Federal court would not entertain jurisdiction on basis of diverse citizenship, where it appeared that transfer of claim was made to corporation organized for the purpose of prosecuting the suits.—Eds.

¹³ Statement abridged and portions of opinion omitted.—Eds.

The facts of this case as stated by the Appellate Court in their opinion are as follows:

"Appellee for many years worked for her living in St. Louis, Missouri, doing housework. Some time prior to this suit, having accumulated the sum of \$1,200.00, she placed it at interest on real estate security, and the note representing the loan came due in January, 1901. At that time appellant was engaged in the real estate and loan business in the city of St. Louis. He was president of the J. T. Donovan Real Estate Company, of which his son, Joseph M. Donovan, was vice-president. The latter was also president of the Fidelity Realty Company, which did business in the same room with the other company, and in which appellant was likewise interested. Shortly after her note became due, appellee took it, and the trust deed by which it was secured, to appellant's place of business, for the purpose of having him collect the money due and re-invest it for her, but at the office she made arrangements to that end with Joseph M. Donovan, whom, she testified, she considered a clerk. In June, 1901, she left the city and did not return until the following October. In the meantime she made arrangements with a friend, Miss Slaterly, to attend to her business. During her absence the note owned by her was collected, and a new one for a like amount secured by deed of trust, was given Miss Slaterly, who afterwards turned the papers over to appellee. The new note was made by the Fidelity Realty Company, by J. M. Donovan, its president, and was payable to the order of George M. Cooper, a clerk in appellant's office, who endorsed the same without recourse. It was secured by a deed of trust upon a 25-foot lot on San Francisco avenue in the city of St. Louis, made by the Fidelity Realty Company to appellant, as trustee. The note and trust deed were dated January 19, 1901, but were not delivered to Miss Slaterly until the following August. With these papers there was also delivered to Miss Slaterly a written guaranty, executed by J. T. Donovan Real Estate Company, by J. T. Donovan, its president, which, after reciting the assignment to appellee of the note and securities in question, proceeded as follows: 'And whereas, there is being erected on said lot of ground, certain improvements, which may not yet be fully completed and paid for; now, therefore, in consideration of said sum of \$1,200.00, we hereby promise and agree to cause said improvements to be fully completed and paid for, and to hold the said Miss Julia Purtell harmless from all loss or damage on account of mechanics' liens, or on account of the failure of the said Fidelity Realty Company to fully complete said improvements, and to pay for the same. For the consideration aforesaid, we further obligate ourselves to hold Miss Julia Purtell and her assigns harmless from all loss on account of said investment, principal or interest.' The guaranty also contains an undertaking on the part of the maker to pay the interest notes in case of default in the payment thereof for a longer period than thirty days, and to purchase the principal

at its face value, with interest added, within six months after default in the payment of the same.

"Some time after appellee received the last named papers she ascertained that the lot described in the deed of trust was vacant; that no improvements were being made, and that it was worth only about \$150.00. She thereupon called upon J. M. Donovan, the president of the Fidelity Realty Company, who offered to give her in exchange other securities, which, on examination, she found to be entirely inadequate to properly secure the debt. She then made a similar demand of appellant and he offered her to substitute some other piece of property for that which appellee had, but, upon examination of the properties named, appellee refused to accept any of them on the ground that the security was wholly insufficient. While negotiations were pending, two of the interest notes were paid by appellant. Appellee testified that, when she asked appellant what security he could give on said notes, he said he could not give her money, but offered to pay her in eighteen months and told her she would not be at any loss, but this appellant denies. Afterwards negotiations ceased, and this suit was brought.

"Upon the trial the appellant * * * introduced the evidence of himself and Joseph M. Donovan. * * * These witnesses were corroborated to some extent by the securities held by appellee, purporting to have been executed by the two corporations above named. On the contrary, appellee * * * testified that she dealt with appellant on account of the confidence she had in him; that his boys, several of whom were in the office, acted just as other clerks; she said, 'I paid all the confidence to Mr. Donovan I could. I would not pay as much to my brothers as I paid to Mr. Donovan, because he was a Catholic and a member of my church and a good living man, as I supposed.' The manner of transacting business at the Donovan office was fully explained by Lydia M. Cooper, who was appellant's stenographer and typewriter from October, 1897, to April, 1903. She testified that the office was a long, narrow room about twenty feet wide and sixty to seventy-five feet long; and that there was a partition in the front like a banking counter, and in the rear there was a place about ten feet square, where a number of different companies known as the J. T. Donovan Real Estate Company, the Fidelity Realty Company, the Cunliff Realty Company, the Fenimore Realty Company, the Cappa Realty Company and the McKinley Company had headquarters; that the different corporations had different presidents, but that appellant was really the man who ran the whole thing; that there were three sons of appellant in the office, and several other clerks; that J. T. Donovan controlled the business of the Fidelity Realty Company; that there was a bookkeeper and cashier in the office; that over the door there was the sign, 'J. T. Donovan Real Estate Company;' that J. M. Donovan 'never made any transaction without J. T. Donovan sanctioned it;' that the Fidelity Realty Company did not have any financial standing, but was simply

gotten up to keep the property out of judgment, so that the property could be sold and transferred without judgment being paid off; that she had heard appellant say so himself; that 'he said there were judgments against these different companies, and he would get up another company and put the property in the name of the new company, in order that it could be transferred, so that there would be no judgment against it;' that he used the property of the companies indiscriminately; that he would settle the debts of the J. T. Donovan Real Estate Company with these properties, no matter to which company they belonged; that the stock of the J. T. Donovan Real Estate Company was all held by members of the family; that Mr. Donovan got the property named in the deed of trust in question for \$325.00, and put a \$1,200.00 loan on it.

"Joseph M. Donovan, when placed upon the witness stand, denied some of the statements made by Miss Cooper but appellant, when placed upon the stand, did not see fit to deny any of them."

MR. JUSTICE MAGRUDER delivered the opinion of the court. * * *

The evidence tends to show that, although the appellant and his sons turned over to appellee these worthless securities in exchange for her money, yet that appellant himself received the money, and used it for his own private purposes, and sought to escape personal liability by covering up the transaction in the name of a corporation, which was entirely under his own control. This being so, the trial court committed no error in refusing to instruct the jury to find the issues for the defendant. It would have been improper to give such instruction, in view of the fact that the evidence tended to prove that the appellant received the money, and declined to pay it over.

This suit is not brought upon the notes, executed by the Fidelity Realty Company. Those notes and the trust deed securing them were tendered back to the appellant upon the trial, and, upon his refusal to receive them, placed in the custody of the court for the use and benefit of appellant. The object of the suit is to recover, under the common counts, the money actually received by the appellant.

The instructions, given by the court to the jury on behalf of the appellee, submitted to the jury the question of fact, whether the affairs of the J. T. Donovan Real Estate Company and the Fidelity Realty Company were controlled by J. T. Donovan for the transaction of his private business, and whether or not he personally controlled both of these corporations when they received the appellee's money, and whether or not her money was received for appellant's own private individual uses and purposes. The instructions also left it to the jury to find, whether or not the appellant was conducting his business in the name of the J. T. Donovan Real Estate Company, and, through that company, received appellee's money and appropriated the same to his own use and gave her, in payment of it, the

worthless securities above referred to. The judgments of the lower courts, finding for the appellee, settle these questions of fact, so far as we are concerned, against the appellant.

Appellant was president of the J. T. Donovan Real Estate Company, and his son, Joseph M. Donovan, was the vice-president of that company, and Joseph M. Donovan, the appellant's son, was the president of the Fidelity Realty Company. Both of these concerns were controlled, managed and dominated by the appellant, J. T. Donovan. The officer or controlling manager of a corporation cannot use it, and its name, for the transaction of his own private business, and to escape personal liability on his part. The theory, upon which the appellant defends this suit, is that the liability to appellee was not his liability, but that of the corporation known as the Fidelity Realty Company.

In *Hoffman v. Reichert*, 147 Ill. 274, it was held that the directors of a private corporation have no right under any circumstances to use their official position for their own individual benefit.

In the case of *Bank v. Trebein Co.*, 59 Ohio St. 316, it was said: "The fiction, by which an ideal legal entity is attributed to a duly formed incorporated company, existing separate and apart from the individuals composing it, is of such general utility and application, as frequently to induce the belief that it must be universal, and be in all cases adhered to, although the greatest frauds may thereby be perpetrated under the fiction as a shield. But modern cases, sustained by the best text writers, confine the fiction to the purposes for which it was adopted—convenience in the transaction of business and in suing and being sued in its corporate name, and the continuance of its rights and liabilities, unaffected by changes in its corporate members; and have repudiated it in all cases where it has been insisted on as a protection to fraud, or any other illegal transaction."

In *Cook on Corporations* (5th ed., sec. 663), it is said: "A corporation is often organized to act as a 'cloak' for frauds. Such cases as these are becoming common, and the courts are becoming more and more inclined to ignore the corporate existence, when necessary, in order to circumvent the fraud." (See also *Lachman v. Martin*, 139 Ill. 450.) In *Morse on Banks and Banking* (vol. 1—4th ed.—sec. 128) it is said: "If bank directors do not manage the affairs and business of the bank according to the directions of the charter, and in good faith, they will be liable to make good all losses, which their misconduct may inflict upon either stockholders or creditors, or both. * * * They may be held to account to an injured party in a court of chancery, or they or any of their number, who shared in the wrong-doing, may be sued at law for damages." So, in the case at bar, appellant, as an officer of one or more of the corporations here involved, was guilty of such a fraud in transferring to appellee these worthless securities in payment of the money which he owed her, that he can be held liable personally for the loss inflicted upon her.

Even if the corporation be regarded as the real debtor, and the appellant as only its agent, yet inasmuch as he was guilty of fraud perpetrated upon appellee, the law will hold him liable. In 1 American and English Encyclopedia of Law (2d ed., p. 1135), it is said: "An agent will be held personally liable to third persons for all damages, sustained by them in consequence of any fraudulent or malicious acts committed by him on behalf of his principal, and, in an action against the agent for fraud, the fact that he derived no personal profit or benefit therefrom is immaterial." In *Ree v. Peterson*, 91 Ill. 288, it is said: "In an action at law for damages, the fact that a defendant acted throughout in the capacity of agent, in a fraud perpetrated by him, will afford him no excuse." (See also *Seddon v. Connell*, 10 Simons 86; *Windram v. French*, 151 Mass. 549.)

It is claimed, on the part of the appellant, that the court below erred in permitting appellee to prove that the appellant promised to repay the money to her. It is said that this was a promise to pay the debt of a third person, to-wit: of the Fidelity Realty Company, and that, under the Statute of Frauds, the promise to pay the debt of a third person must be in writing. The statute of the state of Missouri in relation to the Statute of Frauds upon this subject, which is almost identical with our own, was introduced in evidence over the objection of appellee. It was not pleaded as a defense; and the general rule is that, where the statute of another state is relied upon as a defense, it must be pleaded as set out, at least in substance, and must be proved on the trial, and, if it is not pleaded, it is error to permit it to be proved. (*Palmer v. Marshall*, 60 Ill. 289.) But whether or not this rule applies here, where the declaration contained merely the common counts, and did not set up any contract, makes no difference under the circumstances of this case, because the proof tends to show that, when appellant received appellee's money, he was not conducting business under a bona fide corporate organization, but was using a corporate entity for the transaction of his private business, and, as he was, therefore, personally liable to the appellee for the repayment of her money, his promise was to pay his own debt, and not the debt of a third person.

It is said that the court erred in the admission of certain testimony, introduced by the appellee. We are satisfied with the following statement upon this subject, made by the Appellate Court in their opinion deciding this case, to-wit: "Appellant also claims that the court erred in permitting appellee to show the course of business pursued by him, his exercise of control over the various companies in the same office, and the indiscriminate manner, in which he used the money of said companies, and in admitting evidence, tending to show the reason why the appellee had special confidence in him. In our opinion, this evidence was all proper, as bearing upon the question whether the appellant was really conducting his own business under the name of the several corporations for his own benefit, and also whether he took advantage of appellee's special confidence in

him to use her money, and give her securities, which were practically worthless."

The objection is made that a recovery cannot be had in this kind of case under the common counts. We are unable to concur in this contention. In *Wilson v. Turner*, 164 Ill. 398, this court said (p. 403): "An action for money had and received will lie whenever one person has received money which, in justice, belongs to another, and which, in justice and right, should be returned. * * * When, therefore, according to this rule, one person obtains the money of another which it is inequitable or unjust for him to retain, the person entitled to it may maintain an action for money had and received for its recovery." Inasmuch as, in the case at bar, there was evidence, tending to show that appellant had obtained money from appellee, which it was unjust and inequitable for him to retain, she is entitled to maintain the present action for the recovery of such money. * * *

For the reasons above stated, we are of the opinion that the judgments of the lower courts were correct. Accordingly, the judgment of the Appellate Court, affirming that of the circuit court, is affirmed.¹⁴

GRAMOPHONE AND TYPEWRITER, LIMITED, v. STANLEY.

L. R. (1906) 2 K. B. 856. L. R. (1908) 2 K. B. 89.¹⁵

CASE stated by the Commissioners of Internal Revenue.

At a meeting of the Commissioners of the General Purposes of the Income Tax Acts, held January 22, 1903, the Gramophone and Typewriter, Limited, an English company registered under the Companies Act (hereinafter called the appellant company), appealed against an assessment for the year ending April 5, 1902, of £79,348.

The directors of the appellant company, in accordance with the requirements contained in its articles of association, presented their annual report to the shareholders. From that report a total credit balance appeared of £79,348, which balance was appropriated in manner set forth in the report, and the whole of which was included in the assessment appealed against. It was admitted on the hearing of the appeal that the entire sum was liable to be taxed, except as to

¹⁴ See *Attorney-General v. Great Northern Ry. Co.* (1860) 1 Drew. & S. 154, 6 Jur. (N. S.) 1006; *Keokuk Elec. Ry. &c. Co. v. Weisman* (1910) 146 Ia. 679, 126 N. W. 60; *Des Moines Gas Co. v. West* (1878) 50 Ia. 16; *Chicago Union T. Co. v. Chicago* (1902) 199 Ill. 579, 65 N. E. 470; *Home Fire Ins. Co. v. Barber* (1903) 67 Neb. 644, 93 N. W. 1024; *Stockton v. Central R. Co.* (1892) 50 N. J. Eq. 52, especially at 75-6, 24 Atl. 964; *Weston Elec. Inst. Co. v. Empire Elec. Inst. Co.* (1910) 177 Fed. 1006, 100 C. C. A. 670.—Eds.

¹⁵ Statement abridged and rewritten. Arguments and portions of opinions omitted.—Eds.

£15,000 thereof, a sum stated in the report to have been transferred "to patents account, Germany, in accordance with German law."

This sum of £15,000 concerns the appellant company in respect of its interest in a German company. The Deutsche Grammophon Aktiengesellschaft, hereinafter referred to as the German company, was constituted on January 30, 1900, in conformity with the German law, with its head office in Berlin and among those who united in forming it was the Gramophone Company, Limited, now taken over by the appellant company. The appellant company now holds all the shares of the German company; the members of the board of management of the German company are also directors of the appellant company, and the members of the board of supervision of the German company are nominees of the appellant company.

In the report of the directors of the appellant company the whole of the profits of the German company are brought in in one sum, but of that amount the sum of £15,000—equivalent to the deterioration during the year of the value of the patents purchased by the German company, since these patents at the time of its constitution had three years to run—was, pursuant to German law, transferred to a depreciation fund.

It was contended on behalf of the appellant that this sum, provided out of the earnings of the German company and transferred to the patents account, was not chargeable with income tax.

The Commissioners *held*, (1) that the English company controlled the German company from England; (2) that the entire business of the German company was carried on by, and was the business and property of, appellant company and that the profits of the German company were its profits; that this sum of £15,000 was profits of the appellant company; and that all the profits of the German company should be assessed without regard to the mode of application of such profits. And they confirmed the assessment.

WALTON, J.—This is an appeal from a determination of the Commissioners of Income Tax, and comes before me upon a special case.

The facts upon which this question arises are set out in the case, but I shall state them quite shortly and in chronological order, which I think will make them more intelligible. On January 30, in the year 1900, a company, which I shall call the German company, was incorporated and registered in Germany in accordance with German law, and amongst those who united in forming it was the Gramophone Company, Limited. The German company was constituted under a deed of association a joint stock company with limited liability in conformity with German law. My attention was called to the provisions of the German law, and although, of course, they are not identical with the English law on the subject of limited liability companies, I think their effect is that the German company, constituted in the way which I have described, was a corporation in the same sense, and for all the purposes of the present case as an English limited liability company.

I may refer to Article 178 of the German Commercial Code, which

provides that: "All members of a limited liability company participate in the share capital of the company without being held personally liable for the obligations of the company." Article 210 says: "A limited liability company has, as such, rights and duties; it can acquire real property and other rights over real property, sue and be sued." Article 211 says: "The obligation of a shareholder is limited to payment of the nominal value of his share, and the issuing price when such price is above its nominal value." Article 213 is: "Shareholders cannot demand back their money; they have only a right during the duration of the company to net profit, unless such distribution is prohibited either by the law or by the articles." Referring to the articles of association, which are annexed to the case, and to some extent set out in the special case, I find that by Article 12 the official bodies of the company are: (a) The general meeting of shareholders; (b) the board of supervision; and (c) the board of management. By Article 30 of the articles of association, the business year comprises the period from September 1 to August 31 of the following year. "The board of management has to determine every year, with the sanction of the board of supervision, how much shall be written off annually from the book value of the immovable and movable property. With regard to the depreciation of the patents, at least one-third of the working profit remaining after deduction of all the business expenses shall, before anything is written off the immovable property, be devoted to writing off amounts on patents or similar accounts. The balance-sheet is to be made up to August 31." Then, after some further regulations with regard to the balance-sheet, by Article 33 it is provided: "The net profit remaining, after writing off all depreciation and setting aside all reserves and carrying forward any sum to new account, shall be distributed as follows: (1) In the first place the shareholders shall receive a dividend up to 4 per cent. on the paid-up share capital; (2) the board of supervision shall then receive a percentage of 6 per cent. of the remainder; (3) the rest shall be distributed as a further dividend." The effect of all this is—and I do not think I need go into any further detail for the purposes of this case—that the constitution of a German limited liability company is very similar to that of an English limited liability company, and the position of the shareholders and their relation to the company are very similar in principle to those of the shareholders of an English limited liability company in their relation to the company. The property of the company is not the property of the shareholders; it is the property of the company. The interest of the shareholders in profits is not an interest in the actual profits of the company directly, but an interest only in such dividends as may be from time to time declared.

The German company, as I have stated, was constituted on January 30, 1900, and one of the founders was the Gramophone Company, Limited. On December 10, 1900, the appellant company was registered, and one of its objects was to acquire and take over as a going concern the business and undertaking of the Gramophone

Company, Limited, and all or any of the assets and liabilities of the proprietors of such business and undertaking. The appellant company did, as I understand, take over the assets, business, and undertaking of the Gramophone Company, Limited, and no doubt in so doing took over a large interest which the Gramophone Company, Limited, had in the German company. The result is thus stated in the case: "The appellant company now holds all the shares of the German company, and the members of the board of management of the German company are also directors of the appellant company, and the members of the board of supervision of the German company are nominees of the appellant company,"—nominees as I understand, in this sense: that as the appellant company holds in its own name, or the names of its nominees, all the shares of the German company, they have a controlling voice in the election of all officers of the German company.

In the year in question the total profits of the German company amounted to 79,348*l.* 10*s.* 10*d.* On the hearing of the appeal by the commissioners it was admitted "that the whole of the sum of 79,348*l.* 10*s.* 10*d.* was liable to be taxed under Sched. D, except as to 15,000*l.*, part thereof, a sum stated in the report to have been transferred 'to patents account, Germany, in accordance with German law.' This sum of 15,000*l.*, transferred to patents account to meet the requirements of the German law, concerns the appellant company in respect of their interest in the German company hereinafter referred to." That is to say, the German company, in making up its balance-sheet for the year in question, stated its total profits as 79,348*l.*, but of that amount 15,000*l.* was, in accordance with the regulations which I have read, transferred to a depreciation fund with reference to the patent rights belonging to the German company.

The question is whether the appellant company is chargeable to income tax in respect of that 15,000*l.* The appellant company have no doubt received their dividends arising from the profits of the German company; but the English company has not received this sum of 15,000*l.* It is part of the profits made by the German company; but is an amount which has not been distributed as dividend by that company, but has been placed to reserve to meet depreciation. The question is whether the English company is chargeable in respect of that 15,000*l.* It is said that, inasmuch as the English company owns all the shares of the German company, the business of the German company is the business of the English company, and therefore that the profits of the German company, the 79,348*l.* 10*s.* 10*d.*, are profits earned by the English company. In the case of *Kodak, Ltd., v. Clark* (1) a similar question to this arose. The cases bearing upon questions of this kind were in that case very fully considered by Phillimore, J., and I do not think it is necessary for me to refer to them now. I do not think the case of *Kodak, Ltd., v. Clark* (1)

decides the present question. It seems to me there may be found dicta in the judgments of Phillimore, J., and of the Court of Appeal which appear sometimes in favor of one side and sometimes rather in favor of the other, upon the very point which I have now to determine, but it seems to me they do not bind me. There are two questions involved in the present case. Those two questions are: Whose was the business carried on by the German company? Was it the business of the English company? If it was not the business of the English company, then it seems to me that this appeal must be allowed. But even assuming that it was the business of the English company, then it would be necessary to consider whether that business was controlled or managed by the appellant company in England. If it was their business, and if it was controlled by the appellant company from England, then they would be chargeable in respect of the profits of the foreign business to income tax in England. The important question here seems to me to be this: Was the business of the foreign company the business of the appellant company? There is no doubt that a person in England (I include in the term "person", of course, a company) may be the owner of a commercial undertaking in a foreign country. Such person in England may carry on the foreign business by means of an agent abroad. The agent abroad may be a company, and the owner of the business in England may be a shareholder in that company. If that be so, then the business abroad is the business of the person in this country, notwithstanding that the business abroad is carried on by a foreign company. But in such a case one has throughout this fact, that the business abroad is the business of the person in this country. Was that so in this case? What evidence is there of it? To my mind there is no evidence that the business of the German company was the business of the English company except the fact that the English company has become the owner of all the shares in the German company. That does not extinguish the German company. The German company is an existing person and a different entity from the English company, and I think that the effect of the judgment of the House of Lords in the case of *Salomon v. Salomon* (1) is that the fact that the shares of the German company all belong to the English company does not make the German company a mere alias, or a trustee, or an agent for the English company, or for the shareholders in the English company. I do not think I should be usefully occupying time by reading passages from the judgments in that case, but I might refer to what Lord Herschell says at the bottom of pages 42 and 43. It seems to me that there is nothing here upon which I can find that the business of the German company is the business of the English company except the fact that the shares of the German company now all belong to the English company. The effect of that is to make the shareholders in the English company the owners of all the shares in the German company; but it still leaves

(1)—(1897) A. C. 22.

their relationship to the German company that of shareholders to the company, and does not constitute that company their agent or trustee. That seems to me to have been clearly decided in the case of *Salomon v. Salomon* (1), and, therefore, I do not think that there is any evidence to show that these profits were the profits of the appellant company. They had an interest in them and upon that interest they have been taxed, and there is no dispute as to that. To that extent, no doubt, they are liable. Beyond that, it appears to me they are not liable, and, therefore, this appeal should succeed.

Judgment accordingly.

From the above decision, the surveyor of taxes appealed to the Court of Appeal.

In affirming the opinion of the court below :

COZENS-HARDY, M. R.—The German company was established in Germany in 1900 in accordance with German law. It was undoubtedly a company with several shareholders, who brought in considerable capital. One of those shareholders was an English company whose undertaking was subsequently acquired by the present English company. At some date, which is not stated, the English company acquired all the shares of the German company, and I assume in favor of the Crown that this event had happened before the material dates. The fact that an individual by himself or his nominees holds practically all the shares in a company may give him the control of the company in the sense that it may enable him by exercising his voting powers to turn out the directors and to enforce his own views as to policy, but it does not in any way diminish the rights or powers of the directors, or make the property or assets of the company his, as distinct from the corporation's. Nor does it make any difference if he acquires not practically the whole, but absolutely the whole, of the shares. The business of the company does not thereby become his business. He is still entitled to receive dividends on his shares, but no more. I do not doubt that a person in that position may cause such an arrangement to be entered into between himself and the company as will suffice to constitute the company his agent for the purpose of carrying on the business, and thereupon the business will become, for all taxing purposes, his business. Whether this consequence follows is in each case a matter of fact. In the present case I am unable to discover anything in addition to the holding of the shares which in any way supports this conclusion. The German company was not at first, and there is no evidence that it has ever become, a sham company or a mere cloak for the English company. It has its board of management and its board of supervision as required by the German law. Its accounts are made out in accordance with German law. On the other hand the English company has its board of directors, some of whom are on the German board. It has a proper account and balance-sheet, in which its interest in the German company is described accurately as

so many shares in the German company, and the gross profits of the German company are in no way brought into the profit and loss account of the English company.

FLETCHER MOULTON, L. J.—The present case requires us to examine a more difficult question, namely, that of an individual corporator who owns the whole of the stock of the corporation. According to English law it is not possible for an individual corporator to be the legal owner of the whole of the stock of a company of this kind so as legally to be the sole shareholder, inasmuch as the company would by English law cease to exist if the number of corporators fell below a certain standard. But according to German law no such limitation appears to exist, and in the present case the respondents acquired the whole of the shares of the German Gramophone Company, without thereby terminating or interfering with its corporate existence or the legal incidents thereof and it is in consequence of such acquisition that the present dispute arises.

Treating it as an abstract proposition of law, I am of opinion that the acquisition of the whole of the shares of a corporation by one individual does not of itself alter the nature of his relationship to the corporation. His de facto control when he possesses 98 per cent is probably complete from a practical point of view, and although it is no doubt rendered more complete in theory when he possesses himself of the whole of the shares, it is still of the nature of a control exercised by corporators over the corporation, and does not make him and the corporation in any sense identical. The directors of the corporation do not become his agents. Their duties are still controlled by the rules and constitution of the corporation itself. Nor is this consideration one of theoretical law only. The fact that the whole of the shares of the corporation are held by one individual at one moment by no means implies that they will be so held at a future time, and the responsibility of the directors and officers of the corporation is to the corporation itself, whatever be its composition at any moment as to number of corporators. It will be no excuse to them when called to account in the regular way and at the regular periods, according to the constitution of the corporation, to plead that they obeyed the directions of the individual corporators as they existed at a particular moment (unless given in the manner prescribed by the constitution of the corporation), and on the strength of such directions failed to obey the corporate rules.

The German company was not in its inception a "one man" company. It was formed by the coalition of three firms or companies, of which one was a predecessor of the present English company. Its capital consisted of 1,000 shares, of which 540 were held by the then existing English company and the other 460 were held independently. Although, therefore, from the first the English interest in the company was what is often called a "controlling interest," there was a substantial holding in the company in other hands, so that there can be no doubt that initially it was a bona fide German company in which the interest of the English company was only that of holding

shares. From the time of its formation to the date with which we have to deal it has been carried on, so far as appears, in a strictly regular manner as a German company. * * *

*Appeal dismissed.*¹⁰

IN RE RIEGER, KAPNER & ALTMARK.

(District Court, S. D. Ohio, E. D.)

1907. 157 Fed. 609.

IN bankruptcy. On application for extension of receivership.

SATER, District Judge.—On the 17th day of August, 1907, a petition in involuntary bankruptcy was filed in this court against the partnership firm of Rieger, Kapner & Altmark, and Frank Rieger, Jacob Kapner, Adolph Kapner, and Louis Altmark, the four individuals composing such firm. The defendants other than Rieger, who had disappeared, and whose whereabouts was unknown, answered, consenting to an adjudication against them respectively. On the 20th day of August a petition in involuntary bankruptcy was filed in the United States District Court for the Southern District of New York against the same parties, other than Jacob Kapner, who was subsequently, by amendment, brought into the case. Frederick C. McLaughlin was in that case appointed receiver of all of the property of the defendants, and on the 24th day of August he was directed to take possession of the hosiery mills of the Kapner Bros. & Duga Hosiery Company, an Ohio corporation, operating at Zanesville, Dresden, and Frazesburg, Ohio. The alleged bankrupts were restrained at the same time from interfering in any wise with the receiver in his possession and in his taking possession of the property, and this court was requested to assist the receiver in securing and maintaining possession of such property, and to make such ancillary orders as may be proper and requisite.

On the 26th day of August, on application of the petitioners filed in this court, C. T. Marshall and Frederick C. McLaughlin were appointed receivers of all the property belonging to the partnership firm, and directed to take charge of the same. On the same day an application was made to extend the receivership to the property of the above-named corporation, which is alleged to be a subsidiary company to the partnership. The application recites that the capital

¹⁰ *Salomon v. Salomon & Co.*, L. R. (1897) App. Cas. 22, reversing *Broderip v. Salomon*, L. R. (1895) 2 Ch. 323, (One-man Company); *Lange v. Burke* (1901) 69 Ark. 85, 61 S. W. 165; *Wavcross Air-Line R. Co. v. Offerman & Co.* (1900) 109 Ga. 827, 35 S. E. 275; *Ulmer v. Lime Rock R. Co.* (1904) 98 Me. 579, 57 Atl. 1001; *N. Y. Airbrake Co. v. International Steam Pump Co.* (1909) 64 Misc. (N. Y.) 347, 120 N. Y. S. 683; *In Re Watertown Paper Co.* (1909) 169 Fed. 252, 94 C. C. A. 528 (valuable review of authorities), *Accord*. Cf. *Kodak, Ltd. v. Clark*, (1902) 2 K. B. 450, (1903) 1 K. B. 505; *Apthorpe v. Peter Schoenhofen Brewing Co.* (1899) 80 L. T. 395, 4 Tax Cases, 41; *United States Brewing Co. v. Apthorpe* (1898) 4 Tax Cases 17.—Eds.

stock of the corporation is \$50,000, divided into 500 shares, all of which is owned by the partners, which certificates of stock constitute a part of the assets of the alleged bankrupts. Of the stock issued, shares of the face value of \$27,200 are in the possession of McLaughlin as receiver. Other shares of the face value of \$12,300 are held by Edward Moyse & Company, stockbrokers of New York City, who desire the receivers to take possession of the property of the corporation, and the residue of the stock, being the holdings of Jacob Kapner, is said to be held by the Guardian Trust Company, of Pittsburgh, Pa. The application further charges that the confessed bankrupts are in control of the corporate business, that the partnership business which was conducted in the city of New York was abandoned on the 14th day of August, and that if the defendants be permitted to remain in control of the property and assets of the corporation they will remove and dispose of it, to the irreparable damage of the creditors of both the partnership and the corporation. The prayer of the application is that the receivers be given possession of the corporate property as part of the assets of the bankrupts' estate, and that the officers and agents of the corporation be enjoined from disposing of the corporation's property pending the hearing. On August 30th a hearing was had on such application. The corporation and the defendants other than Rieger, who has not appeared, resist the application to extend the receivership to the corporate property, and assert that the corporation has at all times since its organization existed as a separate and distinct entity, and is in no respect subsidiary to the partnership. At the time the proceedings in bankruptcy were commenced, of the 500 shares of authorized capital stock, 490 shares had been issued. Ten shares remained as treasury stock. Jacob Kapner, Louis Altmark, and Frank Rieger each owned 123 shares. R. Kapner, an uncle of Jacob Kapner, owned four shares, and Abe Kapner, the son of Jacob Kapner, owned one share, which share was issued to him two years ago, when he was but 19 years of age. The residue of the issued stock, aggregating 116 shares, was owned by Adolph Kapner. The members of the partnership firm owned 485 shares of the outstanding stock, and relatives of Jacob Kapner owned the remaining 5 shares.

The corporation was organized in 1896, to manufacture hosiery, and was owned by the Kapners and Duga. The partnership was formed in 1901, and engaged in a commission business, selling hosiery and gloves, and in the manufacture of pants and coats. It asserts itself to be the sole agent of the corporation. The firm business was so loosely conducted that neither Altmark, who had charge of the hosiery department, nor Jacob Kapner could give any idea of its debts. The corporation and the firm each kept its own books and bank account, but the business between the corporation and the partnership has been so conducted that the state of accounts between them is in dispute, and, so far as the record shows, is unknown, although the partnership took the corporation's entire product, and the books of either concern ought to show the exact condi-

tion of the two concerns with reference to each other. Jacob Kapner, who was the president and treasurer of the corporation and in charge of its finances, was unable to state even approximately the condition of the account, or how much the corporation owed the firm, whether it was \$60,000 or more. He professes not to know which owes the other, or when the corporation last invoiced. He bought the merchandise, and looked after the raw material for the corporation, and yet states that he does not know what the corporation owes, although, on further inquiry, he testifies that it owes between \$60,000 and \$70,000, in addition to the \$118,000 mortgage given to O'Neal. The secretary, Abe Kapner, testifies that the past-due obligations of the corporation are from \$150,000 to \$200,000. Jacob Kapner first states that he could not recollect who the corporation directors were prior to the 29th day of August, although on that date the board of directors held a meeting at which he presided, and at which one was removed, and three, including himself, went through the formality of resigning. Further examination was required to develop from him that the board consisted of the four partners and his son, Abe. He disclaims knowledge of the firm's assets which are in New York, or an understanding of the firm books. He values the corporation's mills at \$150,000, its trade-mark at \$50,000, and its merchandise at from \$140,000 to \$150,000. Only one of the mills—the one at Dresden—is owned in fee, the other two being leased property. The witness Shore values the mills and machinery at \$150,000. The value of the corporation's trade-mark and merchandise must be regarded as problematical. Jacob Kapner's ignorance, real or professed, about matters with which he ought to have been familiar, if he in fact was not so, reflect seriously on the value of his uncorroborated statements. He was either surprisingly ignorant or forgetful of his own affairs, or willing to conceal the facts regarding them. To meet its pressing obligations, the corporation, on August 20th, executed and delivered to O'Neal a mortgage for \$118,000, securing 46 notes. These notes were negotiated by O'Neal, and the money realized therefrom, excepting about \$6,000 which was due to himself, was advanced to the corporation. To meet its pay rolls it has been transferring its orders and accounts receivable to banks, as security for money advanced for that purpose. It has no bills receivable or outstanding accounts. As fast as these were made, down to the time of the institution of bankruptcy proceedings, they were turned over, sold, to the firm.

Are the partnership and the corporation separate and distinct legal entities, or is one subsidiary and auxiliary to the other? These are the questions to be answered, and, although Jacob Kapner and Altmark repeatedly assert that the partnership is the sole agent of the corporation, and that the two concerns exist and have existed as such entities, these questions must be determined by the court from the facts adduced and the law applicable thereto. Altmark's testimony shows that the corporate stock purchased in 1901 was bought

by the partnership for partnership purposes and to insure to the partnership the control of the product of the corporation's mills.

The partnership owns 99 per cent. of the stock. As the record does not disclose the interest of the respective partners in the firm, the presumption is that they are equal partners; and it is significant that the number of shares of corporate stock standing in the name of each is the same, excepting that the shares accredited to Adolph Kapner are seven less than to each of his co-partners. That Abe Kapner and R. Kapner, son and uncle, respectively, of Jacob Kapner, hold five shares of the stock does not militate seriously against the sole ownership by the members of the firm. In *Bank v. Trebein Co.*, 59 Ohio St. 316, 52 N. E. 834, 4 out of 500 shares of stock were held by Trebein's relatives by blood or marriage, but that fact did not, under the circumstances of that case, deter the court from holding that the corporation was in substance another Trebein. The *Great Western Natural Gas & Oil Co.* was held in *In re Muncie Pulp Co.*, 139 Fed. 546, 71 C. C. A. 530, to be a mere agent of the pulp company, and as having "no shadow of claim to the property" held in its name, notwithstanding the fact that one of its shares of stock was held by a person who was not a party to its organization, as an agent and creation of the pulp company. It is not shown when or how R. Kapner acquired his four shares of stock, or that as a stockholder he ever participated in the corporate affairs. Instead of the partnership being the agent of the corporation, the corporation was the instrumentality acquired by the partnership to supply it with goods for the market. The corporate organization, it is true, was maintained, but it was for the purpose of facilitating and benefiting the partnership business. It was but a mere adjunct of the partnership. The partners acquired the corporate stock, made themselves the directors of the corporation, and owned, operated, and controlled both concerns, and used the corporation's trade-mark on their bill-heads. They shared in the profits made or losses sustained by the company. These four men as directors constituted themselves as partners a selling agency to dispose of their own manufactured product. This is as unusual as it would be for a natural person, doing business in his correct name, to designate himself, or contract with himself, as his own agent regarding another branch of his business conducted by himself under a fictitious name, and to hold himself out to the public as two distinct persons. That he should so represent himself and keep for his two kinds of business separate books and separate bank accounts might give him a double line of credit, and might hinder and delay his creditors in reaching his assets in case of insolvency, but a court of equity, having knowledge of the fact, would have no difficulty in brushing aside the subterfuge and subjecting the whole of his property to the payment of his debts. The four individuals composing the firm may have obtained—doubtless did obtain—a larger credit by operating in two names. That they so used whatever credit was accorded them as to entail loss on many of those who bestowed it is manifest from the record and

their admissions of insolvency. As the corporation was subsidiary to and the mere agency of the partnership, the representation that the partnership is the sole agent of the corporation is untrue and misleading. To deny the individual and partnership creditors participation in the administration of so much of the bankrupts' estate as may be found in possession of the corporation, and to compel such creditors to remain silent spectators until the corporate creditors shall have been paid in full out of the proceeds of the sales of the corporate property, or out of the profits of the business if it should be profitably continued, or until the corporate property is exhausted, is to deny them a right guaranteed by the bankrupt act, and to hinder and delay them in the pursuit of their legal remedies against the bankrupts and their property, and is, consequently, fraudulent in law, however honestly the partners may have intended to deal with their creditors in case of insolvency. *Bank v. Trebein Co.*, 59 Ohio St. 316-325, 52 N. E. 834. The individual partnership creditors have a direct interest in the corporate assets, for, assuming, without deciding, that the innocent corporate creditors must first be paid out of the corporate property, the residue, if any, would pass for administration to the trustee in bankruptcy.

Ind. (The fiction of legal corporate entity cannot be so applied by the partners as to work a fraud on a part of their creditors, or hinder and delay them in the collection of their claims, and thus defeat the provisions of the bankrupt act.) The doctrine of corporate entity is not so sacred that a court of equity, looking through forms to the substance of things, may not in a proper case ignore it to preserve the right of innocent parties or to circumvent fraud. The case of *Re Muncie Pulp Co.*, 139 Fed. 546, 71 C. C. A. 530, is closely in point. The pulp company, which subsequently became bankrupt, caused the incorporation and organization of the Great Western Natural Gas & Oil Company, and the transfer to it of its gas and oil wells and lands. The president and treasurer of the pulp company owned all of the stock of the Great Western Company, though one share was put into the name of a third party for the purpose of having a resident director in Indiana. The Great Western Company was treated as an agent of the pulp company for the development of its business, especially for the supplying of cheap motor power. The pulp company, having become bankrupt, the receiver demanded the delivery to him of the property in the possession of the Great Western Company as a part of the assets of the pulp company. The demand was resisted, but Coxe, Circuit Judge, said:

"The Great Western Company has no shadow of claim to the property in controversy, and to permit it, or its president or shareholders, to dispose of such property is to sanction a fraud upon the creditors of the pulp company. * * * The new oil company was the old company under another name."

The president of the oil company was required to turn over to the receiver the property of the bankrupt in his possession or under his control. In *Interstate Telegraph Co. v. Baltimore & Ohio Telegraph*

Co. (C. C.) 51 Fed. 49, affirmed in 54 Fed. 50, it appears that the railroad company caused the telegraph company to be incorporated, became the sole owner of its stock, selected its own officers and employes as officers of the new company, and represented such company to have authority to contract with reference to its whole railway telegraph system. It was held that the railroad company was not only the actual owner of the telegraph company, but that the latter company was a mere department, or bureau, of the railroad company, created and maintained for the railroad company's benefit as an agent to make contracts. It follows as a corollary that, had the railroad company become insolvent while the telegraph company was in existence, the property in the possession of the telegraph company, notwithstanding its corporate entity, would, if necessary, have been treated as property of the railroad company. The Supreme Court of Ohio has repeatedly ignored the fiction of legal corporate entity when used as a shield for fraudulent or other illegal acts. The rule is clearly stated in *Bank v. Trebein Co.*, 59 Ohio St. 316, 52 N. E. 834, as follows:

"In contemplation of law, a corporation is a legal entity, an ideal person, separate from the real persons who compose it. [This fiction, however, is limited to the uses and purposes for which it was adopted—convenience in the transaction of business, and in suing and being sued in its corporate name, and the continuance of its rights and liabilities, unaffected by changes in its corporate members.] But the fiction cannot be abused. A corporation cannot be formed for the purpose of accomplishing a fraud or other illegal act under the disguise of the fiction; and, when this is made to appear, the fiction will be disregarded by the courts, and the acts of the real parties dealt with as though no such corporation had been formed, on the ground that fraud vitiates everything into which it enters, including the most solemn acts of men. * * * The good faith of the parties to such a transaction must be [determined by its legal effect on the rights of others.] If its legal effect works a fraud on their rights, the finding of a court that the parties acted in good faith is simply an erroneous conclusion of law from the facts."

Other authorities are *Cincinnati Volksblatt Co. v. Hoffmeister*, 62 Ohio St. 189, 200, 56 N. E. 1033, 48 L. R. A. 732, 78 Am. St. Rep. 707; *State v. Standard Oil Co.*, 49 Ohio St. 137, 177-179, 30 N. E. 279, 15 L. R. A. 145, 34 Am. St. Rep. 541; *Brundred v. Rice*, 49 Ohio St. 640, 32 N. E. 169, 34 Am. St. Rep. 589; *Thompson on Corporations*, § 1077; *Cook on Corporations* (4th ed.) p. 23; 7 Am. & Eng. Ency. Law, 633, 634. * * *

An order may be drawn extending the receivership to the property in the possession of the corporation as a part of the assets of the partnership, and vesting in the receivers such power as will preserve the rights of all parties in interest, and prevent, if practicable and if thought best, the stoppage of the business and any result which would depreciate or tend to depreciate the assets. The receivers will take possession of such property, of every nature and

description, and the corporation, its officers, agents, and employes are directed to deliver the same to them.¹⁷

STATE v. STANDARD OIL CO.

1892. 49 Ohio St. 137, 30 N. E. 279.¹⁸

THE state, by its attorney-general, commenced this action to oust the defendant of the right to be a corporation, on the ground that it had abused its corporate franchises, by becoming a party to an agreement that is against public policy. The issues were raised by a demurrer to the answer.

MINSHALL, J.—Three questions arise upon the pleadings: 1. Should the defendant, the Standard Oil Company, be regarded as a party in its corporate capacity, to the agreement constituting the Standard Oil Trust.¹⁹ 2. Had the company power to become a party to such an agreement. 3. If so, is the right of the state to demand a forfeiture of its corporate franchises, or of the power to make and perform such agreements, barred by lapse of time.

1. It will be observed, on reading the answer, that while the defendant denies that it "entered into or became a party to either or both of the agreements in said petition set forth," and also, "denies that it has at any time or in any manner acquiesced in, or observed, performed or carried out either or both of said agreements," it does not deny the averment of the petition, that "all of the owners and holders of its capital stock, including all the officers and directors of said company, signed said agreements." Nor could it have been the intention to do so, as the answer proceeds to admit, "that it," the corporation, "is informed and believes that the individuals named in the agreement, being the same individuals who executed" it, "did enter into the agreements set forth" in the petition; claiming "that said agreements were agreements of individuals in their individual capacity and with reference to their individual property, and were not, nor were they designed to be, corporate agreements." The claim is based upon the argument, that the corporation is a legal entity separate from its stockholders, that in it are vested all the property and powers of the company, and can only be affected by such acts and agreements as are done or executed on its behalf by

¹⁷ *Interstate Telegraph Co. v. Baltimore & Ohio. Tel. Co.* (1892) 51 Fed. 49, aff'd. (1893) 54 Fed. 50, 4 C. C. A. 184; *In Re Muncie Pulp Co.* (1905) 139 Fed. 546, 71 C. C. A. 530, *Accord.*

Cf. Edmunds v. Illinois Central R. Co. (1908) 36 Nat. Corp. Rep. 50.

See *Senior v. New York City R. Co.* (1906) 111 App. Div. (N. Y.) 39, 97 N. Y. S. 645, aff'd., (1907) 187 N. Y. 559, 80 N. E. 1120; *Stone v. Cleveland & C. R. Co.* (1911) 202 N. Y. 352, 95 N. E. 816; *Pullman Palace Car Co. v. Missouri & C. R. Co.* (1885) 115 U. S. 587, 29 L. Ed. 499; and article by I. Maurice Wormser, in 12 *Columbia Law Rev.*, at pp. 502-6.—Eds.

¹⁸ Statement abridged. Arguments omitted.—Eds.

¹⁹ Opinion given in full on first question only.—Eds.

its corporate agencies acting within the legitimate scope of their powers. That its stockholders are not the corporation, that their shares are their individual property, and that they may each and all dispose of and make such agreements affecting their shares, as best suit their private interests; and that no such acts and agreements of stockholders, subservient of their private interests, can be ascribed to the company as a separate entity, though done and concurred in by each and all of the stockholders.

The general proposition that a corporation is to be regarded as a legal entity, existing separate and apart from the natural persons composing it, is not disputed; but that the statement is a mere fiction, existing only in idea, is well understood, and not controverted by any one who pretends to accurate knowledge on the subject. It has been introduced for the convenience of the company in making contracts, in acquiring property for corporate purposes, in suing and being sued, and to preserve the limited liability of the stockholders, by distinguishing between the corporate debts and property of the company, and of the stockholders in their capacity as individuals. All fictions of law have been introduced for the purpose of convenience and to subserve the ends of justice. It is in this sense that the maxim *in fictione juris subsistit aequitas*, is used, and the doctrine of fictions applied. But when they are urged to an intent and purpose not within the reason and policy of the fiction they have always been disregarded by the courts. Broom's Legal Maxims, 130. "It is a certain rule," says Lord Mansfield, C. J., "that a fiction of law shall never be contradicted so as to defeat the end for which it was invented, but for every other purpose it may be contradicted." *Johnson v. Smith*, 2 Burr., 962. "They were invented," says Brinkerhoff, J., in *Wood v. Ferguson*, 7 Ohio St. 291, "for the advancement of justice, and will be applied for no other purpose." And it is in this sense that they have been constantly understood and applied in this state. *Hood v. Brown*, 2 Ohio R., 269; *Rossman v. McFarland*, 9 Ohio St., 381; *Collard's Adm'r v. Donaldson*, 17 Ohio R., 266.

No reason is perceived why the principles applicable to fictions in general, should not apply to the fiction that a corporation is a personal entity, separate from the natural persons who compose it, and for whose benefit it has been invented. One author seems to think that it has outlived its usefulness, that it is "a stumbling-block in the advance of corporation law toward the discrimination of the real rights of actual men and women," and should be abandoned. *Taylor on Corp.*, sec. 51. Among the many attempts that have been made to define the nature of a corporation, that given by Mr. Kyd, discarding, or at least not adopting, the metaphysical distinction of a legal entity separate from the persons composing it, is certainly the most practical, presenting as it does, the real nature of a corporation as seen in its constituents, and, in the manner that it is formed and transacts its business. His definition is, "a collection of many individuals united into one body, under a special denomination, having

perpetual succession under an artificial form, and vested, by the policy of the law, with the capacity of acting, in several respects, as an individual, particularly of taking and granting property, of contracting obligations, and of suing and being sued, of enjoying privileges and immunities in common, and of exercising a variety of political rights, more or less extensive, according to the design of its institution, or the powers conferred upon it, either at the time of its creation, or, at any subsequent period of its existence." 1 Kyd on Corporations, 13. In brief then, a corporation is a collection of many individuals, united in one body under a special denomination, and vested by the policy of the law with the capacity of acting in several respects as an individual. "The statement," says Mr. Morawetz, "that a corporation is an artificial person, or entity, apart from its members, is merely a description, in figurative language, of a corporation viewed as a collective body; a corporation is really an association of persons, and no judicial dictum or legislative enactment can alter this fact." See his work on Corporations, sec. 227. So that the idea that a corporation may be a separate entity, in the sense that it can act independently of the natural persons composing it, or abstain from acting, where it is their will that it shall, has no foundation in reason or authority, is contrary to the fact, and, to base an argument upon it, where the question is, as to whether a certain act was the act of the corporation, or of its stockholders, cannot be decisive of the question, and is therefore illogical; for it may as likely lead to a false, as to a true result.

Now, so long as a proper use is made of the fiction, that a corporation is an entity apart from its shareholders, it is harmless, and because convenient, should not be called in question; but where it is urged to an end subversive of its policy, or such is the issue, the fiction must be ignored, and the question determined, whether the act in question, though done by shareholders, that is to say, by the persons united in one body, was done simply as individuals and with respect to their individual interests as shareholders, or was done ostensibly as such, but, as a matter of fact, to control the corporation and effect the transaction of its business, in the same manner as if the act had been clothed with all the formalities of a corporate act. This must be so, because the stockholders having a dual capacity, and capable of acting in either, and a possible interest to conceal their character when acting in their corporate capacity, the absence of the formal evidence of the character of the act, cannot preclude judicial inquiry on the subject. If it were otherwise, then, in one department of the law, fraud would enjoy an immunity awarded to it in no other.

Therefore, the real question we are now to determine is, whether it appears from the face of the pleadings, giving effect to all the denials of fact contained in the answer, that the execution of the agreement set forth in the petition, should be imputed to the association of persons constituting The Standard Oil Company of Ohio, acting in their corporate capacity.

The agreement provides in the first place that the parties to it shall be divided into three classes, the first class to embrace all the stockholders and members of certain corporations and limited partnerships, the defendant, The Standard Oil Company of Ohio, being one. It is then covenanted by the parties, that, as soon as practicable, a corporation shall be formed in each of certain states, under the laws thereof, Ohio being one, to mine for, produce, manufacture, refine and deal in petroleum and all its products; with the proviso, however, that instead of organizing a new corporation, any existing one "may be used for the purpose when it can advantageously be done," and in Ohio the defendant has been so used.

In a subsequent part of the agreement, nine trustees are selected, their powers and duties are defined, and provision made for the selection of their successors.

As will hereafter appear, it is made the duty of the parties to the agreement, to transfer their stocks or interests in their respective companies or firms to these trustees, who hold the same in trust, but with the power to vote on the same as though the real owners; in consideration of which, trust certificates are issued to the owners, who, as the owners of such certificates, elect the successors of the trustees.

It is then provided that all the property, assets and business of the corporations and limited partnerships embraced in the first class "shall be transferred to and vested in the said several Standard Oil Companies." And in order to accomplish this purpose, it is provided that "the directors and managers of each and all of the several corporations and limited partnerships mentioned in class first, are hereby authorized and directed by the stockholders and members thereof (all of them being parties to this agreement), to sell, assign, transfer, convey and make over, for the consideration hereinafter mentioned, to the Standard Oil Company or companies, of the proper state or states, as soon as said corporations are organized and ready to receive the same, all the property, real and personal, assets and business, of said corporations and limited partnerships."

Now in the case of the defendant, it will be observed, that this contemplated, and could not have been accomplished without, corporate action. The Standard Oil Company of Ohio was required to transfer all its property, assets and business to a new company to be organized in the state; and this was to be accomplished by the obligation imposed on its members and stockholders, all of whom are parties to the agreement, to authorize and require the directors and managers to make the transfer. The property and assets of the corporation could only be transferred by a corporate act, and the agreement could not in this respect, be carried into effect, other than by such corporate act; and clearly indicates that the purpose of the stockholders of the defendant, in becoming a party to it, was to affect their property and business as a corporation; in other words, was to act in their corporate, and not in their individual, capacity.

The subsequent agreement of January 4, 1882, does not materially change the original agreement in this regard: Reciting that "it is not deemed expedient that all of the companies and associations should transfer their property to the said Standard Oil Companies at the present time," and "that it is deemed advisable that a discretionary power should be vested in the trustees as to when such transfer should be made," provides that, "until said trustees should so decide, each of said companies shall remain in existence and retain its property and business, and the trustees shall hold the stock thereof, in trust as in said agreement provided." So that under the agreement as modified, the directors and managers of the defendant may be required by its stockholders and members, all of whom are parties to the agreement, to make the transfer of the property and business of the defendant, whenever the trustees may in their discretion direct. The effectiveness of this provision to secure all intended by it, may be better understood, by observing that "the directors and managers," "the stockholders and members" and "the trustees" here mentioned, are substantially the same persons, occupying these different relations at one and the same time.

It signifies nothing that the transfer here provided for has not, as respects the defendant, been made. It does not change the evidence it affords of the purpose and object of the members of the corporation in becoming parties to the agreement.

Again, the agreement, as performed by the members of the defendant, as effectually places the property and business of the defendant under the control and management of the Standard Oil Trust, as if the same had been transferred as provided in the original agreement. It is averred in the petition, and not denied in the answer, "that prior to the dates of the trust agreements aforesaid, defendant's capital stock consisted of 35,000 shares of \$100 each, and upon the signing of said agreements in the manner aforesaid, 34,993 shares of said stock, belonging to the persons who signed the agreements in manner above set forth (in what proportions, however, plaintiff is unable to state), were transferred, by defendant's transferring officers, upon defendant's stock books, to the certain nine trustees who were appointed and named in the first one of said trust agreements, upon the request of the respective owners of said shares and in pursuance of the provisions of said trust agreements, the remaining seven of said shares of stock being retained by, or transferred to, the directors of defendant company; that at the time said transfer of stock was made, there were seven directors of defendant, and each one of the seven held one share of the stock aforesaid, but the number of said directors was thereafter reduced to five, who still hold and vote said seven shares of stock and no more. That in lieu of the transfer of said 34,993 shares, as aforesaid, to the nine trustees above mentioned, an equal amount, in par value, of certificates of the Standard Oil Trust, which were provided for and described in said trust agreements, was issued and delivered by said nine trustees to the persons aforesaid, from whom said nine trustees

had received said 34,993 shares of stock in defendant company; that the capital stock of said defendant company is still \$3,500,000, and the nine trustees before mentioned still hold and control the 34,993 shares thereof which were transferred to them as above stated."

So that all but seven of the 35,000 shares of the defendant's capital stock have been transferred by the owners, who are parties to the agreement, to the trustees of the Standard Oil Trust; and continue to be held in trust, as appears by the supplemental agreement, the transferrers receiving in lieu thereof trust certificates equal at par value to the par value of the stock received. The control which this gives, and was intended to give, over the business of the defendant, appears from the following provisions contained in the trust agreement:

"It shall be the duty of said trustees to exercise general supervision over the affairs of said several Standard Oil Companies, and as far as practicable over the other companies or partnerships, any portion of whose stock is held in said trust. It shall be their duty as stockholders of said companies to elect as directors and officers thereof faithful and competent men. They may elect themselves to such positions when they see fit so to do, and shall endeavor to have the affairs of said companies managed and directed in the manner they may deem most conducive to the best interests of the holders of said trust certificates."

Thus, the trustees as the legal owners of the stock, may not only elect whom they please, but may elect themselves, as directors of the defendant; and not only may manage, but it is their duty to have "the affairs" of the defendant, managed and directed in the manner they may deem most conducive to the best interests of the holders of the trust certificates. In other words, it is to be managed in the interest of the Standard Oil Trust, whose principal place of business is in New York City, irrespective of what might be its duties to the people of this state, from which it derives its corporate life; and its real stockholders receive their dividends from the profits of that trust, and not from the earnings of their company; for the holders of the trust certificates, received in exchange for their stock transferred to the trustees, remain in law and in equity, the real owners of the stock so transferred; and the averment in the answer that the dividends of the company are paid to the holders of its stock "appearing as such on its stock-books" is immaterial; since these persons are not the owners, but the trustees of the stock. In fact, the averment is simply a part of the evidence, that the company, through its directors, recognizes and performs the agreement on its part. The payment of its dividends to the persons appearing as stockholders on its stock-books is what enables the parties to the agreement to realize the primary object of the trust agreement—the accumulation of the earnings of the various companies, partnerships and individuals named in the agreement, as a common fund from which the holders of the trust certificates are to be paid dividends when declared by the trustees; and whereby many separate interests

being united under one management, form a virtual monopoly through the power acquired of so controlling the production and price of petroleum and its products, as to destroy competition.

Applying then the principle that a corporation is simply an association of natural persons, united in one body under a special denomination, and vested by the policy of the law with the capacity of acting in several respects as an individual, and disregarding the mere fiction of a separate legal entity, since to regard it in an inquiry like the one before us would be subversive of the purpose for which it was invented, is there, upon an analysis of the agreement, room for doubt, that the act of all the stockholders, officers and directors of the company in signing it, should be imputed to them as an act done in their capacity as a corporation? We think not, since thereby all the property and business of the company is, and was intended to be, virtually transferred to the Standard Oil Trust, and is controlled, through its trustees, as effectually as if a formal transfer had been made by the directors of the company. On a question of this kind, the fact must constantly be kept in view, that the metaphysical entity has no thought or will of its own; that every act ascribed to it, emanates from and is the act of the individuals personated by it; and that it can no more do an act or refrain from doing it, contrary to the will of these natural persons, than a house could be said to act independently of the will of its owner; and, where an act is ascribed to it, it must be understood to be the act of the persons associated as a corporation, and whether done in their capacity as incorporators or as individuals, must be determined by the nature and tendency of the act.

It therefore follows, as we think, from the discussion we have given the subject, that where all, or a majority, of the stockholders comprising a corporation, do an act which is designed to affect the property and business of the company, and which, through the control their numbers give them over the selection and conduct of the corporate agencies, does affect the property and business of the company, in the same manner as if it had been a formal resolution of its board of directors; and the act so done is *ultra vires* of the corporation and against public policy, and was done by them in their individual capacity for the purpose of concealing their real purpose and object, the act should be regarded as the act of the corporation; and, to prevent the abuse of corporate power, may be challenged as such by the state in a proceeding in *quo warranto*. * * *

And in this connection, it is proper to say, that, in the judgment of the court, if the company through its directors, or otherwise, should hereafter recognize the transfers of the shares that have been made on its stock-books to the trustees provided for in the trust agreement, or should hereafter make such transfers; or should pay dividends to them instead of to the real owners of the shares; or should permit such trustees to vote on shares so held by them in the election of its directors, in every such case, it must be regarded and

held, as performing the agreement in violation of the judgment of this court.

*Judgment ousting the defendant from the right to make the agreement set forth in the petition and of the power to perform the same.*²⁰

UNITED STATES v. LEHIGH VALLEY RAILROAD COMPANY.

1910. 220 U. S. 257, 55 L. ed. 458, 31 Sup. Ct. 387.

MR. CHIEF JUSTICE WHITE delivered the opinion of the court.

This case is one of what were known as the commodities cases previously decided and reported in *United States v. Delaware & Hudson Co.*, 213 U. S. 366. The controversy now is but a sequel to that disposed of in the previous cases. To understand the question now for consideration it is essential to have in mind the contentions which arose for decision upon the previous appeal and the disposition which was made of them. We therefore refer to those subjects.

The United States proceeded, both by suits in equity and mandamus, against certain railroad companies, including the Lehigh Valley, to prohibit them from transporting coal in interstate commerce in violation of what were deemed to be the prohibitions of the fifth paragraph of the first section of the act to regulate commerce as amended on June 29, 1906, usually referred to as the commodities clause of the Hepburn Act. The clause is as follows:

"From and after May first, nineteen hundred and eight, it shall be unlawful for any railroad company to transport from any state, territory, or the District of Columbia, to any other state, territory, or the District of Columbia, or to any foreign country, any article or commodity, other than timber and the manufactured products thereof, manufactured, mined or produced by it, or under its authority, or which it may own in whole, or in part, or in which it may have any interest, direct or indirect, except such articles or

²⁰*Ford v. Chicago Milk Shippers Assn.* (1895) 155 Ill. 166, 39 N. E. 651; *Distilling & Cattle Feeding Co. v. People* (1895) 156 Ill. 448, 41 N. E. 188 ("Whisky Trust"); *Harding v. American Glucose Co.* (1899) 182 Ill. 551, 55 N. E. 577; *Dunbar v. American Tel. & C. Co.* (1906) 224 Ill. 9, 79 N. E. 423; *State v. Creamery Package Mfg. Co.* (1910) 110 Minn. 415, 126 N. W. 126, 623; *People v. North River Sugar Refining Co.* (1890) 121 N. Y. 582, 24 N. E. 834 ("Sugar Trust"); *Anthony v. American Glucose Co.* (1895) 146 N. Y. 407, 41 N. E. 23. Cf. *Trenton Potteries Co. v. Oliphant* (1899) 58 N. J. Eq. 507, 43 Atl. 723.

See also *Arkansas & Canal Co. v. Farmers' Loan & Co.* (1889) 13 Colo. 587, 22 Pac. 954; *Chicago Union Traction Co. v. City of Chicago* (1902) 199 Ill. 579, 65 N. E. 470; *Sheldon Hat Blocking Co. v. Eickemeyer & Mach. Co.* (1882) 90 N. Y. 607; *Andres v. Morgan* (1900) 62 Ohio St. 236, 56 N. E. 875; *Omaha Hotel Co. v. Wade* (1877) 7 Otto (U. S.) 13, 24 L. ed. 917; *McKinley v. Wheeler* (1889) 130 U. S. 630, 32 L. ed. 1048.—Eds.

commodities as may be necessary and intended for its use in the conduct of its business as a common carrier." 34 Stat. 584, c. 3591.

In effect, the contention of the government was that the clause in question prohibited railroad companies from moving in the channels of interstate commerce articles or commodities other than the articles excepted by the provision which had been manufactured, mined or produced by the companies or under their authority or which were at the time of the transportation owned by them or which had been previously owned by them in whole or in part or in which the companies then or previously had any interest, direct or indirect. The government, moreover, insisted that these general propositions embraced the movement by the companies in interstate commerce of a commodity which had been manufactured, mined or produced by a corporation in which the transporting railroad company was a stockholder, irrespective of the extent of such stock ownership. The railroad companies in effect defended the suits upon the ground that the statute as construed by the government was repugnant to the constitution. Each of the cases was submitted upon bill and answer and petition and return to the Circuit Court of the United States for the eastern district of Pennsylvania, held by three circuit judges under the Expediting Act of February 11, 1903. 32 Stat. 823, c. 544. The submission in each case was made as a result of a stipulation between counsel "that the submission on bill and answer and any averment or admission in the pleadings of either party shall in no wise prejudice the said parties in any other suit or proceeding heretofore or hereafter instituted, and shall be operative and take effect only with respect to the present suit and for the purpose thereof."

Treating the commodities clause in question as having the significance attributed to it by the United States the court held it to be repugnant to the constitution. Judgments and decrees were accordingly entered, denying the applications for mandamus and dismissing the bills of complaint. The reasons which led to this action were expounded in one opinion, made applicable to all the cases, the court briefly but comprehensively stating the facts in each case which were relied upon by the government as bringing the defendant corporation within the clause as the government construed it. The cases were then brought here.

As was done in the lower court, the cases here were all disposed of by one opinion, the facts in each case as summarized by the court below being stated. In deciding the cases it became necessary first to ascertain the meaning of the commodities clause. In performing this duty the conclusion was reached that the clause did not have the far-reaching significance attributed to it by the government and which had been substantially adopted by the court below, but on the contrary had a much narrower meaning. Attention was directed to the fact that the statute disjunctively applied four generic prohibitions, that is, it forbade a railway company from transporting in interstate commerce articles or commodities, 1, which it had manu-

factured, mined or produced; 2, which have been so mined, manufactured or produced under its authority; 3, which it owns in whole or in part; and, 4, in which it has an interest direct or indirect. All these prohibitions, however, were held to have but a common purpose, "that is, the dissociation of railroad companies prior to transportation from articles or commodities, whether the association resulted from manufacture, mining, production or ownership, or interest, direct or indirect."

In coming to determine whether the government was correct in its contention that these prohibitions operated to prevent a railroad company from transporting a product because it was owned by or had been mined, manufactured or produced by a corporation in which the railroad company was the owner of stock, irrespective of the amount of such stock ownership, it was expressly decided that the prohibitions of the statute were addressed only to a legal or equitable interest in the commodities to which the prohibitions referred, that they therefore did not prohibit a railroad company from transporting commodities mined, manufactured, produced or owned by a distinct corporation, merely because the railroad company was the owner of some or all of the stock in such corporation.

Summing up its review as to the true construction of the commodities clause, the court held (p. 415) that it prohibited "a railroad company engaged in interstate commerce from transporting in such commerce articles or commodities under the following circumstances and conditions: (a) When the article or commodity has been manufactured, mined or produced by a carrier or under its authority, and at the time of transportation the carrier has not in good faith before the act of transportation dissociated itself from such article or commodity; (b) When the carrier owns the article or commodity to be transported in whole or in part; (c) When the carrier at the time of transportation has an interest, direct or indirect, in a legal or equitable sense, in the article or commodity, not including, therefore, articles or commodities manufactured, mined or produced or owned, etc., by a bona fide corporation in which the railroad company is a stockholder."

Thus construed, the clause was held to be within the power of congress to enact. As this conclusion rendered it necessary to reverse the action of the court below which had been exclusively predicated upon the unconstitutionality of the statute, the question arose as to what disposition should be made of the cases. That is to say, the constitutionality of the statute being settled and its true meaning being expounded, the question was whether the cases should be finally disposed of or should be left in such a position as to give the government the right to proceed to apply and enforce the prohibitions of the statute against the various corporations which were defendants if it deemed a good case existed for so doing. Disposing of this subject in the light of the consent upon which the cases had been tried in the court below, and of the error which had obtained as to the true meaning of the statute and of the consequent concentration of

the attention of the court and of the parties to the question of the constitutionality of the statute, instead of its application to the facts, when correctly construed, it was determined that the decree should not conclude the right of the United States in the respective causes to further proceed to enforce the statute as construed, and hence that that subject should be left open for future action. Referring to this matter, it was said (p. 418):

"As the court below held the statute wholly void for repugnancy to the constitution, it follows from the views which we have expressed that the judgments and decrees entered below must be reversed. As, however, it was conceded in the discussion at bar that in view of the public and private interests which were concerned, the United States did not seek to enforce the penalties of the statute, but commenced these proceedings with the object and purpose of settling the differences between it and the defendants concerning the meaning of the commodities clause and the power of congress to enact it as correctly interpreted, and upon this view the proceedings were heard below by submission upon the pleadings, we are of opinion that the ends of justice will be subserved, not by reversing and remanding with particular directions as to each of the defendants, but by reversing and remanding with directions for such further proceedings as may be necessary to apply and enforce the statute as we have interpreted it."

Accordingly, the mandate of this court provided that the cause "be, and the same is hereby, remanded to the said Circuit Court for further proceedings in conformity with the opinion of this court."

Upon the filing of the mandate the court below vacated its decree dismissing the bill in this (the equity) cause, and reinstated the case upon the docket. The United States then presented an amended bill and asked leave to file it. The amendment contained copious averments in regard to the actual relations existing between the railroad company and one of the coal companies mentioned in the original bill, viz., the Lehigh Valley Coal Company. In substance it was averred that as to this particular coal company the railroad company was not only the owner of all the stock issued by the coal company, but that the railroad company so used the power thus resulting from its stock ownership as to deprive the coal company of all real, independent existence and to make it virtually but an agency or dependency or department of the railroad company. In other words, in great detail facts were averred which tended to establish that there was no distinction in practice between the coal company and the railroad company, the latter using the coal company as a mere device to enable the railroad company to violate the provisions of the commodities clause. It was expressly charged that in consequence of these facts:

"The coal company is not a bona fide mining company, but is merely an adjunct or instrumentality of the defendant. The defendant is in legal effect the owner of and has a pecuniary interest

in the coal mined by the coal company, and which is transported by the defendant."

Not only was it thus charged that the railroad company used its stock ownership to so commingle the operating of the affairs of the mining company with its own as to render it impossible to distinguish as a matter of fact between them, but it was moreover expressly in substance charged that exerting its influence as the owner of all the stock of the coal company the railroad company caused the coal company to buy up all the coal produced by other mining companies in the area tributary to the railroad and fix the price at which such coal was bought so as to control the same and the transportation thereof and establish the price at which the coal thus ostensibly acquired by the coal company by purchase should be sold when it reached the seaboard.

It was charged that by these abuses the production, shipment and sale of all the coal within the territory served by the railroad company was brought within the dominion of that company practically to the same extent as if it was the absolute owner of the same. Finally it was alleged as follows:

"That by virtue of the facts hereinbefore set out and otherwise, and more particularly by virtue of the control, direction, domination, and supervision exercised by the persons who are the officers of the defendant railroad and by the defendant over all the operations of the said coal company, embracing the mining and production of said coal, the shipment and transportation of the same over the defendant railroad, and the sale thereof at the seaboard, it follows:

"First. That the coal company, not being in substance and in good faith a bona fide corporation, separate from the defendant, but a mere adjunct or instrumentality of the defendant, the defendant, at the time of transportation, has an interest, direct or indirect, in a legal or equitable sense, in said coal.

"Second. That said coal of said coal company is mined and produced under the authority of defendant, and the defendant at the time of transportation and before the act of transportation has not in good faith dissociated itself from all exercise of authority over said coal but continues to exercise authority over said coal at the time of transportation and over the subsequent sale thereof."

On the objection of the railway company the court denied the request of the United States for leave to file the amended bill. The United States then moved for a decree dismissing its original bill without prejudice, and after argument that motion also was denied. Thereupon counsel for the railroad company moved to dismiss the bill absolutely, and upon the statement of counsel for the United States that it "would not proceed any further in view of the fact that the proposed amendment had been disallowed," the court reached the conclusion "that the bill should be dismissed absolutely upon the allegations of the bill and answer." A decree to that effect was entered, and the Government prosecutes this appeal, relying for

reversal upon the error which it is insisted was committed in refusing to allow the proposed amended bill to be filed and in dismissing the suit.

At the threshold it is insisted by the railroad company that the action of the court below in refusing to permit the proposed amendment, however germane that amendment may have been to the cause of action stated in the original bill and even although the subject-matter of the amendment was not foreclosed by our previous decision, is not susceptible of being reviewed, because the allowance of amendments to pleadings is discretionary with a trial court, and the action of the court below in refusing to permit the amendment, even though erroneous, may not be reversed for error unless a gross abuse of discretion was committed. The principle is elementary, but is inapplicable to this case for a twofold reason: First, because the analysis which we have hitherto made of the opinion of this court on the prior hearing makes it certain that the undoubted object was not to foreclose the right of the Government to enforce in the pending causes the commodities clause as correctly construed, and therefore in this regard the discretion of the court below was controlled by the action of this court. Second, because, in view of the express reservations in the opinion and the explicit language of the mandate of this court, the conclusion cannot be escaped that an absolute abuse of discretion resulted from refusing to permit the amendment, even although such abuse was obviously occasioned by a misconception of the character of the action of this court and the scope of the mandate.

It remains only to consider, first, whether the proposed amendment was germane to the original cause of action, and if it was, whether it was foreclosed by our previous decision.

As to the first question. When it is borne in mind that the suit was brought by the Government to enforce as against the defendant the commands of the commodities clause, the fact that the proposed amendment was germane to such cause of action is too apparent to need anything but statement. Indeed, in the argument at bar on behalf of the railroad company this is in effect conceded, since it is insisted that the amendment should not have been allowed, because in substance its averments virtually constituted part of the original cause of action. And we think it is equally clear that the grounds of the amendment were not foreclosed by our former decision. While that decision expressly held that stock ownership by a railroad company in a bona fide corporation, irrespective of the extent of such ownership, did not preclude a railroad company from transporting the commodities manufactured, mined, produced or owned by such corporation, nothing in that conclusion foreclosed the right of the Government to question the power of a railroad company to transport in interstate commerce a commodity manufactured, mined, owned or produced by a corporation in which the railroad held stock, and where the power of the railroad company as a stockholder was used to obliterate all distinctions between the two cor-

porations. That is to say, where the power was exerted in such a manner as to so-commingle the affairs of both as by necessary effect to make such affairs practically indistinguishable and therefore to cause both corporations to be one for all purposes. To what extent the amendment charged this to be the case will become manifest by again particularly considering its averments concerning the use by the railroad company of the coal company as a purchaser of coal, as also the direct charge made in the proposed amendment that by such acts the railroad company was enabled to control all or a greater portion of the coal produced in the region tributary to its road, and thus to dominate the situation and fix the price, not only at which all the coal could be bought, but at which it could be sold at the seaboard for consumption.

That the facts thus averred and the other allegations contained in the proposed amended bill tended to show an actual control by the railroad company over the property of the coal company and an actual interest in such property beyond the mere interest which the railroad company would have had as a holder of stock in the coal company is, we think, clear. The alleged facts, therefore, brought the railroad company, so far as its right to carry the product of the coal company is concerned, within the general prohibitions of the commodities clause, unless for some reason the right of the railroad company to carry such product was not within the operation of that clause. The argument is that the railroad company was so excepted, because any control which it exerted or interest which it had in the product of the coal company resulted from its ownership of stock in that company, and would not have existed without such ownership. The error, however, lies in disregarding the fact that the allegations of the amended bill asserted the existence of a control by the railroad company over the coal corporation and its product, rendered possible, it is true, by the ownership of stock, but which was not the necessary result of a bona fide exercise of such ownership and which could only have arisen through the use by the railroad of its stock ownership for the purpose of giving it, the railroad company, as a corporation for its own corporate purposes, complete power over the affairs of the coal company, just as if the coal company were a mere department of the railroad. Indeed, such a situation could not have existed had the fact that the two corporations were separate and distinct legal entities been regarded in the administration of the affairs of the coal company. Granting this to be the case, however, it is in effect urged, as the railroad company held all the stock in the coal company, and therefore any gain made or loss suffered by that company would be sustained by the railroad company, no harm resulted from commingling the affairs of the two corporations and disregarding the fact that they were separate juridical beings, because ultimately considered they were but one and the same. This, however, in substance but amounts to asserting that the direct prohibitions of the commodities clause ought to have been applied to a case of stock ownership, par-

ticularly to a case where the ownership embraced all the stock of a producing company, and therefore that a mistake was committed by Congress in not including such stock ownership within the prohibitions of the commodities clause. We fail, however, to appreciate the relevancy of the contention. Our duty is to enforce the statute, and not to exclude from its prohibitions things which are properly embraced within them. Coming to discharge this duty it follows, in view of the express prohibitions of the commodities clause, it must be held that while the right of a railroad company as a stockholder to use its stock ownership for the purpose of a bona fide separate administration of the affairs of a corporation in which it has a stock interest may not be denied, the use of such stock ownership in substance for the purpose of destroying the entity of a producing, etc., corporation and of commingling its affairs in administration with the affairs of the railroad company, so as to make the two corporations virtually one, brings the railroad company so voluntarily acting as to such producing, etc., corporation within the prohibitions of the commodities clause. In other words, that by operation and effect of the commodities clause there is a duty cast upon a railroad company proposing to carry in interstate commerce the product of a producing, etc., corporation in which it has a stock interest not to abuse such power so as virtually to do by indirection that which the commodities clause prohibits, a duty which plainly would be violated by the unnecessary commingling of the affairs of the producing company with its own, so as to cause them to be one and inseparable.

Deciding, as we do, that error was committed in denying leave to file the proposed amended bill, *the decree below is reversed and the cause remanded with directions for further proceedings in conformity with this opinion.*²¹

²¹ "If any general rule can be laid down, in the present state of authority, it is that a corporation will be looked upon as a legal entity as a general rule, and until sufficient reason to the contrary appears; but, when the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud, or defend crime, the law will regard the corporation as an association of persons. This much may be expressed without approving the theory that the legal entity is a fiction, or a mental creation; or that the idea of indivisibility or intangibility is a sophism. A corporation, as expressive of legal rights and powers, is no more fictitious or intangible than a man's right to his own home or his own liberty." Sanborn, J., in *United States v. Milwaukee Refrigerator Transit Co.* (1905), 142 Fed. 247, 255, where a dummy corporation was organized to evade the provisions of the Interstate Commerce and Elkins Acts, and the court termed the device adopted "neither new, nor deserving of success." (p. 256.)

See *Brundred v. Rice* (1892) 49 Ohio St. 640, 32 N. E. 169; *Northern Securities Co. v. United States* (1903) 193 U. S. 197, 48 L. ed. 679 (Opinion of Brewer, J.); and 4 *Columbia Law Rev.* 415, 9 *Columbia Law Rev.* 95, articles by G. F. Canfield.—Eds.

Section 2.—Considered in its Relation to the State.

TRUSTEES OF DARTMOUTH COLLEGE v. WOODWARD.

1819. 4 Wheat. (U. S.) 518, 4 L. ed. 629.¹

ERROR to the Superior Court of the State of New Hampshire.

The facts sufficiently appear in the opinion of the Chief Justice.

The opinion of the court was delivered by MARSHALL, CH. J.:

This is an action of trover, brought by the trustees of Dartmouth College against William H. Woodward, in the State Court of New Hampshire, for the book of records, corporate seal, and other corporate property, to which the plaintiffs allege themselves to be entitled.

A special verdict, after setting out the rights of the parties, finds for the defendant, if certain acts of the legislature of New Hampshire, passed on the 27th of June, and on the 18th of December, 1816, be valid, and binding on the trustees without their assent, and not repugnant to the constitution of the United States; otherwise, it finds for the plaintiffs.

The Superior Court of Judicature of New Hampshire rendered a judgment upon this verdict for the defendant, which judgment has been brought before this court by writ of error. The single question now to be considered is, do the acts to which the verdict refers violate the constitution of the United States?

The title of the plaintiffs originates in a charter dated the 13th day of December, in the year 1769, incorporating twelve persons therein mentioned, by the name of "The Trustees of Dartmouth College," granting to them and their successors the usual corporate privileges and powers, and authorizing the trustees, who are to govern the college, to fill up all vacancies which may be created in their own body.

The defendant claims under three acts of the legislature of New Hampshire, the most material of which was passed on the 27th of June, 1816, and is entitled, "an act to amend the charter, and enlarge and improve the corporation of Dartmouth College." Among other alterations in the charter, this act increases the number of trustees to twenty-one, gives the appointment of the additional members to the executive of the state, and creates a board of overseers, with power to inspect and control the most important acts of the trustees. This board consists of twenty-five persons. The president of the senate, the speaker of the house of representatives, of New Hampshire, and the governor and lieutenant-governor of Vermont, for the time being, are to be members *ex officio*. The board is to be completed by the governor and council of New Hampshire,

¹ Statement abridged. Only such portions of the justices' opinions as relate to the nature of a corporation are given. The charter of Dartmouth College is printed in full in the original report.—Eds.

who are also empowered to fill all vacancies which may occur. The acts of the 18th and 26th of December are supplemental to that of the 27th of June, and are principally intended to carry that act into effect.

The majority of the trustees of the college have refused to accept this amended charter, and have brought this suit for the corporate property, which is in possession of a person holding by virtue of the acts which have been stated.

It can require no argument to prove, that the circumstances of this case constitute a contract. An application is made to the crown for a charter to incorporate a religious and literary institution. In the application, it is stated that large contributions have been made for the object, which will be conferred on the corporation as soon as it shall be created. The charter is granted, and on its faith the property is conveyed. Surely in this transaction every ingredient of a complete and legitimate contract is to be found. * * *

It becomes then the duty of the court most seriously to examine this charter, and to ascertain its true character.

From the instrument itself, it appears, that about the year 1754, the Rev. Eleazer Wheelock established at his own expense, and on his own estate, a charity-school for the instruction of Indians in the Christian religion. The success of this institution inspired him with the design of soliciting contributions in England for carrying on, and extending, his undertaking. In this pious work he employed the Rev. Nathaniel Whitaker, who, by virtue of a power of attorney from Dr. Wheelock, appointed the Earl of Dartmouth and others, trustees of the money, which had been, and should be, contributed; which appointment Dr. Wheelock confirmed by a deed of trust authorizing the trustees to fix on a site for the college. They determined to establish the school on Connecticut River, in the western part of New Hampshire; that situation being supposed favorable for carrying on the original design among the Indians, and also for promoting learning among the English; and the proprietors in the neighborhood having made large offers of land, on condition, that the college should there be placed. Dr. Wheelock then applied to the crown for an act of incorporation and represented the expediency of appointing those whom he had, by his last will, named as trustees in America, to be members of the proposed corporation. "In consideration of the premises," "for the education and instruction of the youth of the Indian tribes," etc., "and also of English youth, and any others," the charter was granted, and the trustees of Dartmouth college were by that name created a body corporate, with power, *for the use of the said college*, to acquire real and personal property, and to pay the president, tutors, and other officers of the college, such salaries as they shall allow.

The charter proceeds to appoint Eleazer Wheelock, "the founder of said college," president thereof, with power by his last will to appoint a successor, who is to continue in office until disapproved by the trustees. In case of vacancy, the trustees may appoint a

president, and in case of the ceasing of a president, the senior professor or tutor, *being one of the trustees*, shall exercise the office, until an appointment shall be made. The trustees have power to appoint and displace professors, tutors, and other officers, and to supply any vacancies which may be created in their own body, by death, resignation, removal, or disability; and also to make orders, ordinances and laws, for the government of the college, the same not being repugnant to the laws of Great Britain, or of New Hampshire, and not excluding any person on account of his speculative sentiments in religion, or his being of a religious profession different from that of the trustees.

This charter was accepted, and the property both real and personal, which had been contributed for the benefit of the college, was conveyed to, and vested in, the corporate body.

From this brief review of the most essential parts of the charter, it is apparent, that the funds of the college consisted entirely of private donations. It is, perhaps, not very important, who were the donors. The probability is, that the Earl of Dartmouth, and the other trustees in England, were, in fact, the largest contributors. Yet the legal conclusion, from the facts recited in the charter, would probably be, that Dr. Wheelock was the founder of the college. * * *

Whence, then, can be derived the idea, that Dartmouth College has become a public institution, and its trustees public officers, exercising powers conferred by the public for public objects? Not from the source whence its funds were drawn; for its foundation is purely private and eleemosynary. Not from the application of those funds; for money may be given for education, and the persons receiving it do not, by being employed in the education of youth, become members of the civil government. Is it from the act of incorporation? Let this subject be considered..

A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence. These are such as are supposed best calculated to effect the object for which it was created. Among the most important are immortality, and, if the expression may be allowed, individuality; properties, by which a perpetual succession of many persons are considered as the same, and may act as a single individual. They enable a corporation to manage its own affairs, and to hold property without the perplexing intricacies, the hazardous and endless necessity, of perpetual conveyances for the purpose of transmitting it from hand to hand. It is chiefly for the purpose of clothing bodies of men, in succession, with these qualities and capacities, that corporations were invented, and are in use. By these means, a perpetual succession of individuals are capable of acting for the promotion of the particular object, like one immortal being. But this being does not share in the civil government of the country,

unless that be the purpose for which it was created. Its immortality no more confers on it political power, or a political character, than immortality would confer such power or character on a natural person. It is no more a state instrument, than a natural person exercising the same powers would be. If, then, a natural person, employed by individuals in the education of youth, or for the government of a seminary in which youth is educated, would not become a public officer, or be considered as a member of the civil government, how is it, that this artificial being, created by law, for the purpose of being employed by the same individuals for the same purposes, should become a part of the civil government of the country? Is it because its existence, its capacities, its powers, are given by law? Because the government has given it the power to take and to hold property in a particular form, and for particular purposes, has the government a consequent right substantially to change that form, or to vary the purposes to which the property is to be applied? This principle has never been asserted or recognized, and is supported by no authority. Can it derive aid from reason?

The objects for which a corporation is created are universally such as the government wishes to promote. They are deemed beneficial to the country; and this benefit constitutes the consideration, and, in most cases, the sole consideration of the grant. In most eleemosynary institutions, the object would be difficult, perhaps unattainable, without the aid of a charter of incorporation. Charitable, or public-spirited individuals, desirous of making permanent appropriations for charitable or other useful purposes, find it impossible to effect their design securely, and certainly, without an incorporating act. They apply to the government, state their beneficent object, and offer to advance the money necessary for its accomplishment, provided the government will confer on the instrument which is to execute their designs the capacity to execute them. The proposition is considered and approved. The benefit to the public is considered as an ample compensation for the faculty it confers, and the corporation is created. If the advantages to the public constitute a full compensation for the faculty it gives, there can be no reason for exacting a further compensation, by claiming a right to exercise over this artificial being a power which changes its nature, and touches the fund, for the security and application of which it was created. There can be no reason for implying in a charter, given for a valuable consideration, a power which is not only not expressed, but is in direct contradiction to its express stipulations.

From the fact, then, that a charter of incorporation has been granted, nothing can be inferred which changes the character of the institution, or transfers to the government any new power over it. The character of civil institutions does not grow out of their incorporation, but out of the manner in which they are formed, and the objects for which they are created. The right to change them is not founded on their being incorporated, but on their being the instruments of government, created for its purpose. The same institu-

tions, created for the same objects, though not incorporated, would be public institutions, and, of course, be controllable by the legislature. The incorporating act neither gives nor prevents this control. Neither, in reason, can the incorporating act change the character of a private eleemosynary institution. * * *

This is plainly a contract to which the donors, the trustees, and the crown, (to whose rights and obligations New Hampshire succeeds), were the original parties. It is a contract made on a valuable consideration. It is a contract for the security and disposition of property. It is a contract, on the faith of which, real and personal estate has been conveyed to the corporation. It is then a contract within the letter of the constitution, and within its spirit also, unless the fact, that the property is invested by the donors in trustees for the promotion of religion and education, for the benefit of persons who are perpetually changing, though the objects remain the same, shall create a particular exception, taking this case out of the prohibition contained in the constitution.

(The learned chief justice held that the legislative acts of New Hampshire, under which the defendant held, impaired the obligation of the charter and were, therefore, unconstitutional, involving a violation of the clause of the United States Constitution (art 1, sec. 10) which prohibits a state from making any law impairing the obligation of contracts.)

MR. JUSTICE WASHINGTON. * * *

What is a contract? It may be defined to be a transaction between two or more persons, in which each party comes under an obligation to the other, and each reciprocally acquires a right to whatever is promised by the other. Under this definition, says Mr. Powell, it is obvious, that every feoffment, gift, grant, agreement, promise, &c., may be included, because in all there is a mutual consent of the minds of the parties concerned in them, upon an agreement between them respecting some property or right that is the objection of the stipulation. He adds, that the ingredients requisite to form a contract, are, parties, consent, and an obligation to be created or dissolved: these must all concur, because the regular effect of all contracts is on one side to acquire, and on the other to part with, some property or rights; or to abridge, or to restrain natural liberty, by binding the parties to do, or restraining them from doing, something which before they might have done, or omitted. If a doubt could exist that a grant is a contract, the point was decided in the case of *Fletcher v. Peck*, (6 Cranch, 87) in which it was laid down, that a contract is either executory or executed; by the former, a party binds himself to do or not to do a particular thing; the latter is one in which the object of the contract is performed, and this differs in nothing from a grant; but whether executed or executory, they both contain obligations binding on the parties, and both are equally within the provisions of the constitution of the United States, which forbids the state governments to pass laws impairing the obligations of contracts.

If, then, a grant be a contract, within the meaning of the constitution of the United States, the next inquiry is, whether the creation of a corporation by charter, be such a grant, as includes an obligation of the nature of a contract, which no state legislature can pass laws to impair?

A corporation is defined by Mr. Justice Blackstone (2 Bl. Com. 37) to be a franchise. "It is," says he, "a franchise for a number of persons, to be incorporated and exist as a body politic, with a power to maintain perpetual succession, and to do corporate acts, and each individual of such corporation is also said to have a franchise, or freedom." This franchise, like other franchises, is an incorporeal hereditament, issuing out of something real or personal, or concerning or annexed to, and exercisable within a thing corporate. To this grant, or this franchise, the parties are, the king, and the persons for whose benefit it is created, or trustees for them. The assent of both is necessary. The subjects of the grant are not only privileges and immunities, but property, or, which is the same thing, a capacity to acquire and to hold property in perpetuity. Certain obligations are created, binding both on the grantor and the grantees. On the part of the former, it amounts to an extinguishment of the king's prerogative to bestow the same identical franchise on another corporate body, because it would prejudice his prior grant. It implies, therefore, a contract not to re-assert the right to grant the franchise to another, or to impair it. There is also an implied contract, that the founder of a private charity, or his heirs, or other persons appointed by him for that purpose, shall have the right to visit, and to govern the corporation, of which he is the acknowledged founder and patron, and also, that in case of its dissolution, the reversionary right of the founder to the property, with which he had endowed it, should be preserved inviolate.

The rights acquired by the other contracting party are those of having perpetual succession, of suing and being sued, of purchasing lands for the benefit of themselves and their successors, and of having a common seal, and of making by-laws. The obligation imposed upon them, and which forms the consideration of the grant, is that of acting up to the end or design for which they were created by their founder. Mr. Justice Buller, in the case of the *King v. Passmore* (3 T. R. 246), says, that the grant of incorporation is a compact between the crown and a number of persons, the latter of whom undertake, in consideration of the privileges bestowed, to exert themselves for the good government of the place. If they fail to perform their part of it, there is an end of the compact. The charter of a corporation, says Mr. Justice Blackstone (2 Bl. Com. 484), may be forfeited through negligence, or abuse of its franchises, in which case the law judges, that the body politic has broken the condition upon which it was incorporated, and thereupon the corporation is void.

It appears to me, upon the whole, that these principles and authorities prove, incontrovertibly, that a charter of incorporation is a contract.

MR. JUSTICE STORY. * * *

It will be necessary, however, before we proceed to discuss these questions, to institute an inquiry into the nature, rights, and duties of aggregate corporations at common law; that we may apply the principles, drawn from this source, to the exposition of this charter, which was granted emphatically with reference to that law.

An aggregate corporation at common law is a collection of individuals united into one collective body, under a special name, and possessing certain immunities, privileges, and capacities in its collective character, which do not belong to the natural persons composing it. Among other things it possesses the capacity of perpetual succession, and of acting by the collected vote or will of its component members, and of suing and being sued in all things touching its corporate rights and duties. It is, in short, an artificial person, existing in contemplation of law, and endowed with certain powers and franchises which, though they must be exercised through the medium of its natural members, are yet considered as subsisting in the corporation itself, as distinctly as if it were a real personage. Hence, such a corporation may sue and be sued by its own members; and may contract with them in the same manner as with any strangers. A great variety of these corporations exist in every country governed by the common law; in some of which the corporate existence is perpetuated by new elections, made from time to time; and in other by a continual accession of new members, without any corporate act. Some of these corporations are, from the particular purposes to which they are devoted, denominated spiritual, and some lay; and the latter are again divided in civil and eleemosynary corporations. It is unnecessary, in this place, to enter into any examination of civil corporations. Eleemosynary corporations are such as are constituted for the perpetual distribution of the free alms and bounty of the founder, in such manner as he has directed; and in this class are ranked hospitals for the relief of poor and impotent persons, and colleges for the promotion of learning and piety, and the support of persons engaged in literary pursuits.

Another division of corporations is into public and private. Public corporations are generally esteemed such as exist for public political purposes only, such as towns, cities, parishes, and counties; and in many respects they are so, although they involve some private interests; but strictly speaking, public corporations are such only as are founded by the government for public purposes, where the whole interests belong also to the government. If, therefore, the foundation be private, though under the charter of the government, the corporation is private, however extensive the uses may be to which it is devoted, either by the bounty of the founder, or the nature and objects of the institution. For instance, a bank created by the government for its own uses, whose stock is exclusively owned by the government, is, in the strictest sense, a public corporation. So a hospital created and endowed by the government for general charity. But a bank, whose stock is owned by private

persons, is a private corporation, although it is erected by the government, and its objects and operations partake of a public nature. The same doctrine may be affirmed of insurance, canal, bridge, and turnpike companies. In all these cases, the uses may, in a certain sense, be called public, but the corporations are private; as much so, indeed, as if the franchises were vested in a single person.

This reasoning applies in its full force to eleemosynary corporations. A hospital founded by a private benefactor is, in point of law, a private corporation, although dedicated by its charter to general charity. So a college, founded and endowed in the same manner, although, being for the promotion of learning and piety, it may extend its charity to scholars from every class in the community, and thus acquire the character of a public institution. This is the unequivocal doctrine of the authorities, and cannot be shaken but by undermining the most solid foundations of the common law. * * *

We are now led to the consideration of the first question in the cause, whether this charter is a contract, within the clause of the constitution prohibiting the States from passing any law impairing the obligation of contracts. In the case of *Fletcher v. Peck*, this court laid down its exposition of the word "contract" in this clause, in the following manner: "A contract is a compact between two or more persons, and is either executory or executed. An executory contract is one, in which a party binds himself to do or not to do a particular thing. A contract executed is one in which the object of the contract is performed; and this, says Blackstone, differs in nothing from a grant. A contract executed, as well as one that is executory, contains obligations binding on the parties. A grant in its own nature amounts to an extinguishment of the right of the grantor, and implies a contract not to re-assert that right. A party is always estopped by his own grant." This language is perfectly unambiguous, and was used in reference to a grant of land by the governor of a state under a legislative act. It determines, in the most unequivocal manner, that the grant of a state is a contract within the clause of the constitution now in question, and that it implies a contract not to re-assume the rights granted. *A fortiori*, the doctrine applies to a charter or grant from the king.

But it is objected, that the charter of Dartmouth College is not a contract contemplated by the constitution, because no valuable consideration passed to the king as an equivalent for the grant, it purporting to be granted *ex mero motu*, and further, that no contracts merely voluntary are within the prohibitory clause. It must be admitted, that mere executory contracts cannot be enforced at law, unless there be a valuable consideration to sustain them; and the constitution certainly did not mean to create any new obligations, or give any new efficacy to nude pacts. But it must, on the other hand, be also admitted, that the constitution did intend to preserve all the obligatory force of contracts, which they have by the general principles of law. Now, when a contract has once passed, *bona fide*,

into grant, neither the king nor any private person, who may be the grantor, can recall the grant of the property, although the conveyance may have been purely voluntary. A gift, completely executed, is irrevocable. The property conveyed by it becomes, as against the donor, the absolute property of the donee; and no such subsequent change of intention of the donor, can change the rights of the donee. And a gift by the crown of incorporeal hereditaments, such as corporate franchises, when executed, comes completely within the principle, and is, in the strictest sense of the terms a grant. Was it ever imagined that land, voluntarily granted to any person by a State, was liable to be resumed at its own good pleasure? Such a pretension would, under any circumstances, be truly alarming; but in a country like ours, where thousands of land titles had their origin in gratuitous grants of the States, it would go far to shake the foundations of the best settled estates. And a grant of franchises is not, in point of principle, distinguishable from a grant of any other property. If, therefore, this charter were a pure donation, when the grant was complete, and accepted by the grantees, it involved a contract, that the grantees should hold, and the grantor should not re-assume the grant, as much as if it had been founded on the most valuable consideration.

But it is not admitted that this charter was not granted for what the law deems a valuable consideration. For this purpose it matters not how trifling the consideration may be; a pepper corn is as good as a thousand dollars. Nor is it necessary that the consideration should be a benefit to the grantor. It is sufficient if it import damage or loss, or forbearance of benefit, or any act done, or to be done, on the part of the grantee. It is unnecessary to state cases; they are familiar to the mind of every lawyer.

(The learned justice after considering the charter in detail, held that there was ample consideration for the contract.)

*Judgment reversed.*²

FIETSAM v. HAY ET AL.

1887. 122 Ill. 293, 13 N. E. 501.

APPEAL from the Circuit Court of St. Clair County; the Hon. B. H. Canby, Judge, presiding.

MR. JUSTICE MULKEY delivered the opinion of the court:

The People's Bank of Belleville, incorporated under a special act of the legislature, approved and in force March 27, 1869, having become insolvent, on the 17th of April, 1878, made a general assignment of all its property and effects for the benefit of creditors. The assignee presented a petition to the County Court of St. Clair

² See article, "A New View of the Dartmouth College Case," by Chief Justice Charles Doe of New Hampshire in 6 Harvard Law Rev. 161, 213.—Eds.

County, at its March term, 1887, for leave to sell "all the rights, privileges, powers and immunities which were granted by the said act incorporating said bank." The judge of the county court being interested in the result of the proceeding, the venue was changed to the Circuit Court of St. Clair County, where, upon due consideration of the petition, that court entered an order dismissing the same. The present appeal is from the order of dismissal.

The correctness of the decision of the circuit court depends entirely upon whether the title to the franchise created and conferred by the bank charter passed as an asset of the bank, to the assignee, under the assignment. That its language is sufficiently comprehensive and adequate to pass the franchise to the assignee, if, as matter of law, the bank could transfer it at all, we have no doubt. This is not questioned. The question, therefore, is, whether a corporate franchise, in the absence of statutory authority, is in law capable of being assigned or transferred. Differently put, the question, as formulated by the parties themselves, is, "Did the franchise of the said bank pass with the deed of assignment to the assignee as a salable asset of the said bank?"

The word "franchise" is often used in the sense of privileges generally, but in its more appropriate and legal sense the term is confined to such rights and privileges as are conferred upon corporate bodies by legislative grant. It is in the latter sense, alone, the word is now to be considered. The franchise proposed to be sold is a corporate franchise, and the artificial body or political entity to which it pertains is what is known to the law as an aggregate corporation. Such a corporation has been well defined to be, "an artificial being created by law, and composed of individuals who subsist as a body politic under a special denomination, with the capacity of perpetual succession, and of acting, within the scope of its charter, as a natural person." Now, a franchise is nothing more than the right or privilege of being a corporation, and of doing such things, and such things only, as are authorized by the corporation's charter. This right of a body of men to be and act as an artificial person, without, as a general rule, incurring individual responsibility, is declared by Blackstone to be "a royal privilege, or branch of the king's prerogative, subsisting in the hands of a subject." (2 Blackstone 37.) Such right of franchise is defined by Bouvier to be "a certain privilege conferred by grant from government, and vested in individuals." (1 Bouvier 545.) Now, it is clear from these definitions, and from the very nature of a corporation, that a franchise, or the right to be and act as an artificial body, vests in the individuals who compose the corporation, and not in the corporation itself. This fact, we think, is not without significance in reaching a conclusion upon the main question to be determined, outside of the numerous authorities bearing directly on the subject.

It will be kept in mind that the corporate body, for purposes of ownership, and, indeed, for most purposes, has a distinct identity from that of the individual corporators. The latter may be wealthy,

when at the same time the former is insolvent, and *vice versa*. The corporation has no right to appropriate, sell, or otherwise dispose of any of the property or effects of a corporator. The relation of debtor and creditor may subsist between them in the same manner as between the company and other persons. The company's entire property may be swept away from it by sequestration, or other means, and yet its franchises will remain vested in the corporators until they are either abandoned or forfeited to the state. All these propositions are familiar to the courts and the profession, and are well sustained by authority.

If, then, the franchise is vested in and belongs to the corporators, and not to the corporation itself, how could the latter transfer and assign it to another? On the plainest of principles this could not be done without legislative authority for that purpose, and we find nothing, either in the statute or the company's charter, conferring such authority. While it is conceded the legislature might confer on the artificial body the power to sell or assign the franchise to strangers, yet this would be, in effect, to authorize it to commit a species of suicide, for it is manifest the corporation could not exist a moment after the franchise conferred upon its members had been transferred to others. Indeed, when we consider the attributes and essential elements of corporate existence, resulting from the grant of the franchise, and without which the artificial body could not accomplish the objects of its creation or perform the duties imposed upon it by law, the sale or assignment of the franchise without special legislative authority would seem to be wholly inadmissible. It is proposed here, it will be noted, to sell simply the franchise of the bank. Assuming this can be done, the question arises, what would be the effect of such a sale? It clearly could not have the effect of making the purchasers, if more than one, an aggregate corporation, with the general banking powers conferred by the bank charter. To assert such a proposition would be simply startling; and yet, if in such case the purchasers would take anything at all, they certainly could not take less than the right to be a banking corporation, with all the powers and privileges conferred by the charter,—for these rights are of the very essence of the franchise; and consequently, the one could not be thus acquired without, by the same act, securing the others,—a view which, as already indicated, has no sanction in reason or authority.

While statements are to be found on this subject in some of the text-books, as well as in some of the decided cases, which cannot be reconciled with the conclusion we have reached, yet we are clearly of opinion that a corporation, in the absence of statutory authority, has no right to sell or transfer its franchise, or any property essential to its exercise, which it has acquired under the law of eminent domain. This proposition, in our judgment, is sustained both by reason and the decided weight of authority. *Black, et al., v. Delaware and Raritan Canal Co.*, 24 N. J. Eq. 455; *Freeman on Execu-*

tions, secs. 179, 180; Pearce on Railroads, 496-1; Jones on Mortgages, sec. 161; Rorer on Judicial Sales (2d ed.), 222; Archer v. Terre Haute and Indianapolis Railroad Co., 102 Ill. 493; Bruffett v. Great Western Railroad Co., 25 Id. 353; Chicago and Rock Island Railroad Co. v. Whipple, 22 Id. 105; Ottawa, Oswego and Fox River Valley Railroad Co. v. Black, 79 Id. 262.

The circuit court having reached this conclusion, its order and judgment will be affirmed.

*Judgment affirmed.*³

Section 3.—Considered With Respect to the Question of Residence or Citizenship.

LOUISVILLE, ETC., R. CO. v. LETSON.

1844. 2 How. (U. S.) 497, 11 L. ed. 353.¹

ERROR to the circuit court of the United States for the district of South Carolina, in an action of covenant brought by Letson, a citizen of New York, against the Louisville, Cincinnati and Charleston Railroad Co., a South Carolina corporation.

The defendants filed a plea to the jurisdiction. A general demurrer to this plea was sustained and defendant appealed.

MR. JUSTICE WAYNE delivered the opinion of the court.

The jurisdiction of the court is denied in this case upon the grounds that two members of the corporation sued are citizens of North Carolina; that the state of South Carolina is also a member, and that two other corporations in South Carolina are members, having in them members who are citizens of the same state with the defendant in error. * * *

A suit then brought by a citizen of one state against a corporation by its corporate name in the state of its locality, by which it

³ "The franchise of becoming and being a corporation, in its nature, is incommunicable by the act of the parties and incapable of passing by assignment. 'The franchise to be a corporation,' said Hoar, J., in *Commonwealth v. Smith*, 10 Allen, 448, 455, 'clearly cannot be transferred by any corporate body of its own will. Such a franchise is not, in its own nature, transmissible'. * * * The essential properties of corporate existence are quite distinct from the franchises of the corporation. The franchise of being a corporation belongs to the corporators, while the powers and privileges, vested in and to be exercised by the corporate body as such, are the franchises of the corporation. The latter has no power to dispose of the franchise of its members, which may survive in the mere fact of corporate existence, after the corporation has parted with all its property and all its franchises." *Matthews, J., in Memphis &c. Railroad Co. v. Railroad Commissioners* (1884) 112 U. S. 609, at page 619; 28 L. ed. 837.

See also *Mercantile Bank v. Tennessee* (1896) 161 U. S. 161, 40 L. ed. 656.—Eds.

¹ Statement rewritten; portions of opinion omitted.—Eds.

was created and where its business is done by any of the corporators who are chosen to manage its affairs, is a suit, so far as jurisdiction is concerned, between citizens of the state where the suit is brought and a citizen of another state. The corporators as individuals are not defendants in the suit, but they are parties having an interest in the result, and some of them being citizens of the state where the suit is brought, jurisdiction attaches over the corporation,—nor can we see how it can be defeated by some of the members, who cannot be sued, residing in a different state. It may be said that the suit is against the corporation, and that nothing must be looked at but the legal entity, and then that we cannot view the members except as an artificial aggregate. This is so, in respect to the subject matter of the suit and the judgment which may be rendered; but if it be right to look to the members to ascertain whether there be jurisdiction or not, the want of appropriate citizenship in some of them to sustain jurisdiction, can not take it away, when there are other members who are citizens, with the necessary residence to maintain it.

But we are now met and told that the cases of *Strawbridge and Curtis*, 3 Cranch, 267, and that of the *Bank of the United States and Deveaux*, 5 Cranch, 84—hold a different doctrine.

We do not deny that the language of those decisions does not justify in some degree the inferences which have been made from them, or that the effect of them has been to limit the jurisdiction of the circuit courts in practice to the cases contended for by the counsel for the plaintiff in error. The practice has been, since those cases were decided, that if there be two or more plaintiffs and two or more joint-defendants, each of the plaintiffs must be capable of suing each of the defendants in the courts of the United States in order to support the jurisdiction, and in cases of corporations to limit jurisdiction to cases in which all the corporators were citizens of the state in which the suit is brought. The case of *Strawbridge and Curtis* was decided without argument. That of the *Bank and Deveaux* after argument of great ability. But never since that case has the question been presented to this court, with the really distinguished ability of the arguments of the counsel in this—in no way surpassed by those in the former. And now we are called upon in the most imposing way to give our best judgments to the subject, yielding to decided cases everything that can be claimed for them on the score of authority except the surrender of conscience.

After mature deliberation, we feel free to say that the cases of *Strawbridge and Curtis* and that of the *Bank and Deveaux* were carried too far, and that consequences and inferences have been argumentatively drawn from the reasoning employed in the latter which ought not to be followed. Indeed, it is difficult not to feel that the case of the *Bank of the United States and the Planters' Bank of Georgia* (9 Wheat., 907) is founded upon principles irreconcilable

with some of those on which the cases already adverted to were founded. The case of the Commercial Bank of Vicksburg and Slocomb (14 Peters, 60) was most reluctantly decided upon the mere authority of those cases. We do not think either of them maintainable upon the true principles of interpretation of the Constitution and the laws of the United States. A corporation created by a state to perform its functions under the authority of that state and only suable there, though it may have members out of the state, seems to us to be a person, though an artificial one, inhabiting and belonging to that state, and therefore entitled, for the purpose of suing and being sued, to be deemed a citizen of that state. We remark, too, that the cases of Strawbridge and Curtis and the Bank and Deveaux have never been satisfactory to the bar, and that they were not, especially the last, entirely satisfactory to the court that made them. They have been followed always most reluctantly and with dissatisfaction. By no one was the correctness of them more questioned than by the late chief justice who gave them. It is within the knowledge of several of us, that he repeatedly expressed regret that those decisions had been made, adding, whenever the subject was mentioned, that if the point of jurisdiction was an original one, the conclusion would be different. We think we may safely assert, that a majority of the members of this court have at all times partaken of the same regret, and that whenever a case has occurred on the circuit, involving the application of the case of the Bank and Deveaux, it was yielded to, because the decision had been made, and not because it was thought to be right. We have already said that the case of Bank of Vicksburg and Slocomb, 14 Peters, was most reluctantly given, upon mere authority. We are now called upon, upon the authority of those cases alone, to go further in this case than has yet been done. It has led to a review of the principles of all the cases. We can not follow further, and upon our maturest deliberation we do not think that the cases relied upon for a doctrine contrary to that which this court will announce, are sustained by a sound and comprehensive course of professional reasoning. Fortunately a departure from them involves no change in a rule of property. Our conclusion, too, if it shall not have universal acquiescence, will be admitted by all to be coincident with the policy of the Constitution and the condition of our country. It is coincident also with the recent legislation of Congress, as that is shown by the act of 28th of February, 1839, in amendment of the acts respecting the judicial system of the United States. We do not hesitate to say, that it was passed exclusively with an intent to rid the courts of the decision in the case of Strawbridge and Curtis. * * *

The case before us might be safely put upon the foregoing reasoning and upon the statute, but hitherto we have reasoned upon this case upon the supposition, that in order to found the jurisdiction in cases of corporations, it is necessary there should be an averment, which, if contested, was to be supported by proof,

that some of the corporators are citizens of the state by which the corporation was created, where it does its business, or where it may be sued. But this has been done in deference to the doctrines of former cases, in this court, upon which we have been commenting. But there is a broader ground upon which we desire to be understood, upon which we altogether rest our present judgment, although it might be maintained upon the narrower ground already suggested. It is, that a corporation created by and doing business in a particular state, is to be deemed to all intents and purposes as a person, although an artificial person, an inhabitant of the same state, for the purposes of its incorporation, capable of being treated as a citizen of that state, as much as a natural person. Like a citizen it makes contracts, and though in regard to what it may do in some particulars it differs from a natural person, and in this especially, the manner in which it can sue and be sued, it is substantially, within the meaning of the law, a citizen of the state which created it, and where its business is done, for all the purposes of suing and being sued. * * *

*Judgment affirmed.*³

DOCTOR v. HARRINGTON.

1904. 196 U. S. 579, 49 L. ed. 606, 25 Sup. Ct. 355.

THE bill in this case was dismissed by the Circuit Court on the ground that it had no jurisdiction upon the fact alleged, and certified to this court the question of jurisdiction. The following is the question certified:

"Whether or not the complainants' bill of complaint showed that there was such diversity of citizenship between the parties complainant and parties defendant in this cause as would be sufficient under the provisions of the United States Revised Statutes to con-

³ See *Marshall v. Baltimore & C. R. Co.* (1853) 16 How. (U. S.) 314, 14 L. ed. 953; *Shaw v. Quincy Mining Co.* (1891) 145 U. S. 444, 36 L. ed. 768.

In *Ohio & C. R. Co. v. Wheeler* (1861) 1 Black (U. S.) 286, Chief Justice Taney said: "This question, as to the character of a corporation, and the jurisdiction of the courts of the United States, in cases wherein they were sued, or brought suit in their corporate name, was again brought before the court in the case of *The Louisville, Cincinnati and Charleston R. Co. v. Letson*, reported in 2 How. (U. S.) 497; and the court in that case, upon full consideration, decided, that where a corporation is created, by the laws of a State, the legal presumption is, that its members are citizens of the State in which alone the corporate body has a legal existence; and that a suit by or against a corporation, in its corporate name, must be presumed to be a suit by or against citizens of the State which created the corporate body; and that no averment or evidence to the contrary is admissible, for the purpose of withdrawing the suit from the jurisdiction of a court of the United States." (p. 296.)—Eds.

fer jurisdiction upon the United States Circuit Court for the Southern District of New York, of this cause."

The court further certified that it entered a decree dismissing the bill, "holding that it appeared from the said bill of complaint that there was no such diversity of citizenship between the parties complainant and defendant as would confer jurisdiction upon the United States Circuit Court for the Southern District of New York in the cause within the meaning of the United States Revised Statutes, and that in arranging the parties to this cause relatively to the controversy the Sol Sayles Company must be grouped on the side of the complainants, with the result that citizens of the same state would thus be parties on both sides of the litigation, and thus deprive this court of jurisdiction."

The bill is very voluminous, and, as it is agreed by appellees that the statement of appellants substantially states its allegation, we quote from appellants' brief as follows:

"This action was brought by the appellants, as stockholders of the Sol Sayles Company; a corporation organized under the laws of the State of New York, for the purpose of vacating and setting aside a judgment obtained by the appellees Harrington against the Sol Sayles Company in the Supreme Court of the State of New York, on October 28, 1902, and the levy and sale under an execution issued thereunder, and of requiring the appellees Harrington to deliver to the Sol Sayles Company certain shares of stock in the Sayles, Zahn Company, and certain bonds, belonging to the Sol Sayles Company, which had been sold under such execution, and for other equitable relief.

"In substance, the complainants allege in their bill of complaint that they are citizens of Morris County, New Jersey; that the defendants Harrington are citizens of the State of New York, and that the defendants Sol Sayles Company and Sayles, Zahn Company are likewise citizens of said state, both being incorporated under the laws of that state; that the Sol Sayles Company was organized with a capital stock of \$100,000, divided into 1,000 shares of the par value of \$100 per share, of which the complainants owned 500 shares and the defendants Harrington 500 shares; that by an arrangement made between the owners of the stock, the voting power on a majority thereof was given to the defendant John J. Harrington, who directed the management of the affairs of the corporation, dictated its policy, and selected its directors; that on January 26, 1898, the defendant John J. Harrington caused the defendant Sayles, Zahn Company to be organized, for the purpose of taking over the business of the defendant Sol Sayles Company and of one Henry Zahn, and thereupon the property of the Sol Sayles Company and of Zahn was transferred to the Sayles, Zahn Company, which likewise was controlled by the defendant John J. Harrington; that the Sol Sayles Company received, in consideration of the transfer of its property, \$50,000 of the capital stock of the

Sayles, Zahn Company, and subsequently subscribed for \$50,000 additional stock.

"It is further alleged that about February 1, 1899, the defendants Harrington, for the purpose of cheating and defrauding the Sol Sayles Company, and the complainants, of their interest in the assets of the Sayles, Zahn Company, fraudulently caused the Sol Sayles Company to execute and deliver to them, without any consideration whatsoever, its promissory notes, aggregating \$23,700, which were utterly fictitious, and thereafter, and on October 3, 1902, the defendants Harrington, in furtherance of their fraudulent scheme, caused an action to be instituted and a judgment to be recovered against the Sol Sayles Company, for the amount of the said promissory notes and interest which was alleged to have accrued thereon, the Sol Sayles Company being in utter ignorance of the nature of the action and omitting to interpose any defense thereto.

"This scheme resulted in the recovery of a judgment against the defendant Sol Sayles Company on October 28, 1902, for \$27,357.28, in favor of the defendants Harrington, who thereupon caused an execution to be issued to the sheriff of the county of New York, against the property and assets of the Sol Sayles Company, under which execution the said sheriff levied on the shares of stock in the Sayles, Zahn Company, and also two bonds of the New Jersey Steamboat Company, which belonged to the Sol Sayles Company, and sold all of the right, title and interest of the Sol Sayles Company in the said certificates of stock and in the said bonds, the said defendants Harrington causing them to be purchased for their own benefit; said shares of stock being then, as the defendants Harrington well knew, and have ever since continued to be, worth upward of \$200,000.

"It further alleged that the complainants caused a demand to be made upon the defendants Harrington, that they transfer the said shares of stock and the said bonds to the Sol Sayles Company, but that they have refused to do so, and have insisted that these shares of stock and bonds are their personal and individual property, and that neither the Sol Sayles Company nor their complainants have any right, title or interest in either the said shares of stock or the said bonds, or any part thereof.

"The twentieth paragraph of the bill of complaint is as follows:

"The complainants were and each of them was a shareholder of the defendant Sol Sayles Company at the time of the transaction herein complained of. This suit is not a collusive one to confer upon a court of the United States jurisdiction of a case of which it would not otherwise have cognizance. The complainants are unable to secure any corporate action on the part of the defendant Sol Sayles Company to redress the wrongs hereinbefore set forth, nor are they able to obtain any redress at the hands of the stockholders of the said defendant Sol Sayles Company. The board of directors of said corporation is under the absolute control and domination

of the defendant John J. Harrington, and the said Harrington, by reason of having possession of a majority of the capital stock of the said corporation, likewise controls the action of the stockholders. Although requested for information with regard to the facts hereinbefore set forth, he has refused to give any information with regard thereto, and has declined to redress the wrongs of which complaint is herein made, or to give to the complainants any opportunity to lay before the board of directors or the stockholders of the defendant Sol Sayles Company the facts herein set forth."

MR. JUSTICE MCKENNA, after stating the case, delivered the opinion of the court.

To sustain the action of the Circuit Court in dismissing the bill the argument is as follows: (1) By a conclusive presumption of law the stockholders of a corporation are deemed to be citizens of the state of the corporation's domicile. (2) Granting that the complainants are citizens of New Jersey, yet as they are suing for the Sol Sayles Company, a New York corporation, that corporation, although in form a defendant, is in legal effect on the same side of the controversy as the complainants, and since it is a citizen of the same state as the other defendants, the Circuit Court had no jurisdiction, as the suit does not involve a controversy between citizens of different states.

1. This is based on the assumption adopted by this court, that stockholders of a corporation are citizens of the state which created the corporation—an assumption physically possible but hardly true in a single instance; and appellants here contend that it should be classed with the fictions of the law and subject to one of their fundamental maxims, and can not be carried beyond the reasons which caused its adoption necessarily requisite. It is, however, more of a presumption than a fiction, but whether we regard it as either it can not be pushed to the end contended for by appellees.

The reason of the presumption (we will so denominate it) was to establish the citizenship of the legal entity for the purpose of jurisdiction in the Federal Courts. Before its adoption difficulties had been encountered, on account of the conditions under which jurisdiction was given to those courts. A corporation is constituted, it is true, of all its stockholders, but it has a legal existence separate from them—rights and obligations separate from them; and may have obligations to them. It can sue and be sued. At first this could be done in the Circuit Court of the United States only when the corporation was composed of citizens of the state which created it. *Bank of United States v. Deveaux*, 5 Cranch, 61; *Hope Insurance Company v. Boardman*, 5 Cranch, 57. But the limitation came to be seen as almost a denial of jurisdiction to or against corporations in the Federal courts, and in Louisville, etc., *Railroad Company v. Letson*, 2 How. 497, prior cases were reviewed; and this doctrine laid down:

"That a corporation created by and doing business in a particular

state, is to be deemed to all intents and purposes as a person, although an artificial person, * * * capable of being treated as a citizen of that state, as much as a natural person." And "when the corporation exercises its powers in the state which chartered it, that is its residence, and such an averment is sufficient to give the Circuit Courts jurisdiction."

The presumption that the citizenship of the corporators should be that of the domicile of the corporation was not then formulated. That came afterwards, and overcame the difficulty and objection that the legal creation, the corporation, could not be a citizen within the meaning of the Constitution. *Marshall v. B. & O. Railroad Company*, 16 How. 314. This, then, was its purpose, and to stretch beyond this is to stretch it to wrong. It is one thing to give to a corporation a status, and another thing to take from a citizen the right given him by the Constitution of the United States. Disregarding the purpose of the presumption, it is easy to represent it, as counsel does, as illogical if not extended to every stockholder; but as easy it would be to show its falseness if so applied. But such charges and countercharges are aside from the question. To the fact and place of incorporation the law attaches its presumption for a special purpose. Perhaps, as intimated in *St. Louis & San Francisco Railway v. James*, 161 U. S. 545, 563, this "went to the very verge of judicial power." Against the further step urged by appellee we encounter the Constitution of the United States.

2. The ninety-fourth rule in equity contemplates that there may be, and provides for, a suit brought by a stockholder in a corporation founded on rights which may properly be asserted by the corporation. And the decisions of this court establish that such a suit, when between citizens of different states, involves a controversy cognizable in a Circuit Court of the United States. The ultimate interest of the corporation made defendant may be the same as that of the stockholder made plaintiff, but the corporation may be under a control antagonistic to him, and made to act in a way detrimental to his rights. In other words, his interests, and the interests of the corporation, may be made subservient to some illegal purpose. If a controversy hence arise, and other conditions of jurisdiction exist, it can be litigated in a Federal court. * * *

Decree reversed.^a

^a A corporation, incorporated under the laws of a state divided into more than one Federal district is a citizen and *inhabitant* of that district within which the general business of the corporation is done and where it has its headquarters and general offices. *Galveston &c. R. Co. v. Gonzales* (1893) 151 U. S. 496, 38 L. ed. 248.

In *Paul v. Virginia* (1868) 8 Wall. (U. S.) 168, 19 L. ed. 357, *held*, a corporation is not a citizen within the meaning of Art. IV, sec. 2, of the Federal Constitution, which declares that "the citizens of each state shall be entitled to all the privileges and immunities of citizens of the several states." See also *Ducat v. City of Chicago* (1868) 48 Ill. 172.

In *Santa Clara County v. Southern Pac. R. Co.* (1886) 118 U. S. 394, 30 L. ed. 118, *held*, the provision in the 14th Amendment to the Constitution,

Section 4.—The Corporation as Distinguished from a Joint-Stock Association.

LIVERPOOL INS. CO. v. MASSACHUSETTS.

1870. 10 Wall. (U. S.) 566, 19 L. ed. 1029.

ERROR to the Supreme Judicial Court of Massachusetts; the case being this:

A statute of the state just named imposes upon "each fire, marine, and fire and marine insurance company, *incorporated* or *associated* under the laws of any government or state other than one of the United States, a tax of 4 per cent. upon all premiums charged or received on contracts made in this commonwealth for insurance of property." The same statute imposes a tax of but 2 per cent. upon such premiums when the company is incorporated under the laws of any one of the United States other than Massachusetts; upon which premiums, where the company is incorporated by itself, it imposes but 1 per cent.; while no tax is imposed by the laws of the state upon the business of insurances transacted by any natural persons citizens of the same.

With the enactment just mentioned on its statute book, the state of Massachusetts, in 1868, filed a bill in its Supreme Judicial Court against the Liverpool and London Life and Fire Insurance Company (a company doing a large business in that state), to collect a tax of 4 per cent. on its premiums upon contracts made in Massachusetts for insurance of property, and to restrain the company from doing further business till the tax was paid. The company set up that it was not "incorporated" at all, but was an association, under the laws of Great Britain, of natural persons, some of whom were citizens and residents of the country just named; and some citizens and residents of the state of New York; formed for the purpose of conducting the business of insurance under certain deeds of settlement, and having the legal character of a partnership; that accordingly it could not be taxed as a "company *incorporated* under the laws of any government or state other than one of the United States;" while, in so far as the discriminating tax of 4 per cent. was sought to be laid against it as a company *associated* simply and not incorporated, it violated, in regard to the members of the company who were subjects of Great Britain, a provision in the treaty of 1815, between that country and the United States, by which it is agreed that the merchants and traders of each nation respectively

which forbids a state to deny to any *person* within its jurisdiction the equal protection of the laws, applies to corporations.

In *Hale v. Henkel* (1905) 201 U. S. 43, 50 L. ed. 652, *held*, a corporation is entitled to immunity under the 4th Amendment affirming "the right of the *people* to be secure in their *persons*" against unreasonable searches and seizures.—Eds.

shall enjoy the most complete protection and security for their commerce; and—in regard to the citizens of New York, that provision in section 2, article 4, of the Federal Constitution which secures to the citizens of each state all the privileges and immunities of citizens in the several states.

Of course, if the company was a corporation, the defence failed; and it not being denied that the persons composing the company were British subjects, with certain citizens of New York with rights like theirs, the first question and the only one if it was resolved affirmatively—was whether the company was a corporation or not.

The Supreme Judicial Court of Massachusetts gave a decree against the company, and enjoined it from the further prosecution of its business till the taxes found to be due were paid. The case was now brought to this court.

MR. JUSTICE MILLER delivered the opinion of the court.

The case of *Paul v. Virginia*, 8 Wallace (U. S.) 168, decided that the business of insurance, as ordinarily conducted, was not commerce, and that a corporation of one state, having an agency by which it conducted that business in another state, was not engaged in commerce between the states.

It was also held in that case that a corporation was not a citizen within the meaning of that clause of the Constitution, which declares that the citizens of each state shall be entitled to all the privileges and immunities of citizens in the several states, and that a corporation created by a state could exercise none of the functions or privileges conferred by its charter in any other state of the Union, except by the comity and consent of the latter.

These propositions dispose of the case before us, if plaintiff is a foreign corporation, and was, as such, conducting business in the state of Massachusetts, and we proceed to inquire into its character in this regard.

The institution now known as the Liverpool and London Life and Fire Insurance Company, doing an immense business in England and in this country, was first organized at Liverpool by what is there called a deed of settlement, and would here be called articles of association.

It will be seen by reference to the powers of the association, as organized under the deed of settlement, legalized and enlarged by the acts of Parliament, that it possesses many, if not all, the attributes generally found in corporations for pecuniary profit which are deemed essential to their corporate character.

1. It has a distinctive and artificial name by which it can make contracts.

2. It has a statutory provision by which it can sue and be sued in the name of one of its officers as the representative of the whole body, which is bound by the judgment rendered in such suit.

3. It has provision for perpetual succession by the transfer and

transmission of the shares of its capital stock, whereby new members are introduced in place of those who die or sell out.

4. Its existence as an entity apart from the shareholders is recognized by the act of Parliament which enables it to sue its shareholders and be sued by them.

The subject of the powers, duties, rights, and liabilities of corporations, their essential nature and character, and their relation to the business transactions of the community, have undergone a change in this country within the last half century, the importance of which can hardly be overestimated.

They have entered so extensively into the business of the country, the most important part of which is carried on by them, as banking companies, railroad companies, express companies, telegraph companies, insurance companies, etc., and the demand for the use of corporate powers in combining the capital and the energy required to conduct these large operations is so imperative, that both by statute, and by the tendency of the courts to meet the requirements of these public necessities, the law of corporations has been so modified, liberalized and enlarged, as to constitute a branch of jurisprudence with a code of its own, due mainly to very recent times. To attempt, therefore, to define a corporation, or limit its powers by the rules which prevailed when they were rarely created for any other than municipal purposes, and generally by royal charter, is impossible in this country and at this time.

Most of the states of the Union have general laws by which persons associating themselves together, as the shareholders in this company have done, become a corporation.

The banking business of the states of the Union is now conducted chiefly by corporations organized under a general law of Congress, and it is believed that in all the states the articles of association of this company would, if adopted with the usual formalities, constitute it a corporation under their general laws, or it would become so by such legislative ratification as is given by the acts of Parliament we have mentioned.

To this view it is objected that the association is nothing but a partnership, because its members are liable individually for the debts of the company. But however the law on this subject may be held in England, it is quite certain that the principle of personal liability of the shareholders attaches to a very large proportion of the corporations of this country, and it is a principle which has warm advocates for its universal application when the organization is for pecuniary gain.

So also it is said that the fact that there is no provision either in the deed of settlement or the acts of Parliament for the company suing or being sued in its artificial name forbids the corporate idea. But we see no real distinction in this respect between an act of Parliament, which authorized suits in the name of the Liverpool

and London Fire and Life Insurance Company, and that which authorized suit against that company in the name of its principal officer. If it can contract in the artificial name and sue and be sued in the name of its officers on those contracts, it is in effect the same, for process would have to be served on some such officer even if the suit were in the artificial name.

It is also urged that the several acts of Parliament we have mentioned expressly declare that they shall not be held to constitute the body a corporation.

But whatever may be the effect of such a declaration in the courts of that country, it cannot alter the essential nature of a corporation or prevent the courts of another jurisdiction from inquiring into its true character, whenever that may come in issue. It appears to have been the policy of the English law to attach certain consequences to incorporated bodies, which rendered it desirable that such associations as these should not become technically corporations. Among these, it would seem from the provisions of these acts, is the exemption from individual liability of the shareholder for the contracts of the corporation. Such local policy can have no place here in determining whether an association, whose powers are ascertained and its privileges conferred by law, is an incorporated body.

The question before us is whether an association, such as the one we are considering, in attempting to carry on its business in a manner which requires corporate powers under legislative sanction, can claim, in a jurisdiction foreign to the one which gave those powers, that it is only a partnership of individuals.

We have no hesitation in holding that, as the law of corporations is understood in this country, the association is a corporation, and that the law of Massachusetts, which only permits it to exercise its corporate function in that state on the condition of payment of a specific tax, is no violation of the Federal Constitution or of any treaty protected by said Constitution.

MR. JUSTICE BRADLEY:

Whilst I agree in the result which the court has reached, I differ from it on the question whether the company is a corporation. I think it is one of those special partnerships which are called joint-stock companies, well known in England for nearly a century, and cannot maintain an action or be sued as a corporation in this country without legislative aid. But as it is a company associated under the laws of a foreign country, it comes within the scope of the Massachusetts statute, and cannot claim exemption from its operation for the causes alleged in that behalf. It could not have been the intent of the treaty of 1815 to prevent the states from imposing taxes or license laws upon either British corporations or joint-stock companies desiring to establish banking or insurance business therein. And certainly these companies cannot be exempted from such

laws on the ground that citizens of other states have chosen to take some of their shares.

*Judgment affirmed.*¹

EDWARDS v. WARREN LINOLINE & GASOLINE WORKS.

1897. 168 Mass. 564, 47 N. E. 502, 38 L. R. A. 791.

Trustee Process.

LATHROP, J.—It is conceded by the plaintiff that, as the jurisdiction of the court depends upon charging the Walworth Mfg. Co. as trustee, inasmuch as there was no service upon the principal defendant, the action was properly dismissed upon discharging the trustee.

The question then is whether the trustee was properly discharged and this depends upon whether the principal defendant, an association formed under the laws of the state of Pennsylvania, is a partnership or a corporation.

The trustee's answers to interrogatories refer to Brightly's Purdon's Digest (12th ed.), 1086-1088, and to the cases of Eliot v. Himrod, 108 Pa. St. 569, and Sheble v. Strong, 128 Pa. St. 315, as containing the law relative to the statement in the answer, that the principal defendant was a partnership, and not a corporation.

From the Digest it appears that such an association is styled a "partnership association," and not a corporation. By the terms of the various acts which have been passed upon the subject, such an association may be formed by three or more persons. The capital is alone to be liable for the debts. There is no personal liability of the members, except to the extent of any unpaid subscription, if certain provisions of the act are complied with. "Interests in such partnership associations" are declared to be personal estate, and are transferable, under such rules and regulations as shall from time to time be prescribed; but if there are no such rules and regulations, the transferee of any interest in any such association is not entitled to any participation in the subsequent business of the association, unless elected to membership therein by a vote of a majority

¹ Tide-Water Pipe Co. v. Assessors (1895) 57 N. J. L. 516, 31 Atl. 220; Edgeworth v. Wood (1896) 58 N. J. L. 463, 33 Atl. 940. *Accord.* See also Andrews Bros. Co. v. Youngstown Coke Co. (1898) 86 Fed. 585, 30 C. C. A. 293 (per Lurton, J.)

"It may be true, as has been argued, that the legislature intended to make a legal being and give it all the essential attributes of a corporate body, and yet that it should not be a corporation. That, the legislature could not do. I do not refer to any *written* constitution. The constitution of things—the order of nature—forbids it. Human powers are not equal to the task of changing a thing by merely changing its name." Bronson, J., in *People v. Assessors* (1841) 1 Hill (N. Y.) 616, at 623.—Eds.

of the members in number and value of their interests. ⁴The business is to be conducted by a board of managers. ⁵The duration of the association may be fixed by the articles of association, but is not to exceed twenty years.

Power to adopt and use a common seal is given in case the association has occasion to execute a deed of conveyance or bonds and mortgages. Land sold to the association, or by it, is required to be conveyed in the name of the association. It is further provided: "Said association shall sue and be sued in their association name; and when suit is brought against any such association, service thereof shall be made upon the chairman, secretary, or treasurer thereof; which service shall be as complete and effective as if made upon each and every member of such association."

In *Eliot v. Himrod*, 108 Pa. St. 569, 580, it is said by Mr. Justice Trunkey, in delivering the opinion of the court: "The formation of a limited partnership association is materially different from the creation of a corporation. Such association is treated in the statute as a partnership which, upon the performance of certain acts, shall possess specified rights and immunities. In contemplation that the association may consist of many members, for convenience it is clothed with many of the features and powers of a corporation, such as the right to sue and be sued, grant and receive, in the association name. But no man can purchase the interest of a member and participate in the subsequent business, unless by a vote of a majority of the members in number and value of their interests. No charter is granted to the persons who record their statement." *Sheble v. Strong*, 128 Pa. St. 315, 318, is to the same effect.

If the question presented were an open one in this commonwealth, it might well be held that such an association could be considered to have so many of the characteristics of a corporation that it might be treated as one.

At common law, a joint stock company formed for business purposes is considered in this commonwealth merely as a partnership. *Tappan v. Bailey*, 5 Met. 529; *Tyrrell v. Washburn*, 6 Allen 466.

The same rule has been applied to joint stock associations formed under the laws of the state of New York, which do not differ, in any essential respect, from the laws of Pennsylvania. *Taft v. Ward*, 106 Mass. 518, and 111 Mass. 518. *Bodwell v. Eastman*, 106 Mass. 525, 526. *Gott v. Dinsmore*, 111 Mass. 45, 51. *Boston & Albany Railroad v. Pearson*, 128 Mass. 445. See also *Frost v. Walker*, 60 Maine, 468; *Dinsmore v. Philadelphia & Reading Railroad*, 32 Leg. Int. 388, and 11 Phila. 483.

In *Taft v. Ward*, 106 Mass. 518, 524, speaking of the New York statutes, it was said by Chief Justice Chapman:

"These statutes provide, in substance, that any association, consisting of seven or more shareholders or associates, may sue and be sued in the name of the president or treasurer; that in such a suit judgment may be rendered against the company; and until an exe-

cution is issued against the company, and returned unsatisfied, no action shall be maintained against individuals. These statutes seem to apply to all copartnerships consisting of seven or more members. The members of such companies are authorized to hold their interests in shares, which are assignable like shares of stock in a corporation, and the action against the members is regarded as supplementary to the action against the company. *Waterbury v. Merchants' Union Express Co.*, 50 Barb. 157. *Robbins v. Wells*, 1 Robertson, 666.

"So far as these statutes relate to the procedure in courts for the recovery of debts, they are limited to the state of New York; for each state adopts its own forms of remedy. Story, *Confl. Laws*, secs. 556-558. The plaintiff could not in this commonwealth bring an action against the president or secretary, and obtain a judgment against the company by its name; nor could he bring an action against the members, or any of them, as a supplement to such an action. In order to do so, we must hold that the statutes of New York prescribing forms of action are in force here. In this commonwealth, such a company is a mere copartnership."

There is nothing inconsistent with an association being a partnership that it has shares, or that the shares are transferable, or that the death of a member shall not work a dissolution of the partnership. *Phillips v. Blatchford*, 137 Mass. 510. See also *Hoadley v. County Commissioners*, 105 Mass. 519; *Gleason v. McKay*, 134 Mass. 419.

The case mostly relied upon by the plaintiff is *Liverpool Ins. Co. v. Massachusetts*, 10 Wall. 566, which was taken to the Supreme Court of the United States on a writ of error from this court. See *Oliver v. Liverpool & London Ins. Co.*, 100 Mass. 531.

(After stating the case, the court proceeded.) In the Supreme Court of the United States, the decree of this court was affirmed, on the ground that the company was a foreign corporation; but Mr. Justice Bradley, while agreeing in the result, differed on the question whether the company was a corporation. He was of opinion that it was one of those special partnerships called joint stock companies, and that it could not sue or be sued in this country without legislative aid.

This view of Mr. Justice Bradley is in accord with the view of this court, and we are not aware that the view taken by the Supreme Court of the United States has been followed in this commonwealth. The decisions which we have already cited show that a foreign joint stock company is considered as an association or partnership, and not as a corporation.

An examination of the statutes further shows that the legislature has clearly recognized the distinction between foreign corporations and associations; and that where it has deemed it best that an act should apply to an association as well as to a corporation, it has said so in plain language. * * *

Many other instances of legislation might be given where the

distinction between a corporation proper and a mere association or organization is shown to be clearly in mind.

Unless the principal defendant can be considered a corporation, it cannot be sued here under the name which the laws of Pennsylvania authorize it to use. Such laws have no extra-territorial force or effect. The trustee, therefore, was properly discharged.

In the opinion of a majority of the court, the order discharging the trustee and dismissing the action must be

*Affirmed.*²

ROUNTREE v. ADAMS EXPRESS CO.

1908. 165 Fed. 152, 91 C. C. A. 186.³

APPEAL from the Circuit Court of the United States for the Western District of Missouri.

Before HOOK and ADAMS, Circuit Judges, and AMIDON, District Judge.

AMIDON, District Judge.—We cannot enter upon the consideration of any of the interesting questions raised in this case and argued by counsel with distinguished ability, for the reason that it appears upon the face of the bill that the trial court was without jurisdiction of the cause. The basis of jurisdiction is the diversity of citizenship of the parties. The bill alleges that the Adams Express Company is a "joint-stock company" duly organized and existing under the laws of the state of New York, and a citizen of that state, and that the defendant is a citizen of the state of Missouri. The averment that the complainant is a joint-stock company is not equivalent to the statement that it is a corporation. This precise question was presented to the Supreme Court in the case of *Chapman v. Barney*, 129 U. S. 677, 9 Sup. Ct. 426, 32 L. ed. 800. That was a suit brought by the United States Express Company in the name of its president. It was described, as the complainant here is, as a joint-stock company, organized under and by virtue of the law of the state of New York, and a citizen of that state. The court of its own motion took cognizance of this defect, and reversed the judgment below, with direction to dismiss the case. Speaking to this point, the court said:

"On looking into the record, we find no satisfactory showing as to the citizenship of the plaintiff. The allegation of the amended petition is that the United States Express Company is a joint-stock

² *People v. Rose* (1905) 219 Ill. 46, 76 N. E. 42; *Frost v. Walker* (1872) 60 Me. 468; *Taft v. Ward* (1871) 106 Mass. 518, (1873) 111 Mass. 518; *State v. Adams Exp. Co.* (1900) 66 Minn. 271, 68 N. W. 1085, *Accord.* See *Tide Water Pipe Co. v. Assessors* (1895) 57 N. J. L. 516, 31 Atl. 220; *Westcott v. Fargo* (1875) 61 N. Y. 542; *Hybart v. Parker* (1858) 4 C. B., N. S. 209.—Eds.

³ Statement abridged.—Eds.

company organized under a law of the state of New York, and is a citizen of that state. But the express company cannot be a citizen of New York within the meaning of the statutes regulating jurisdiction unless it be a corporation. The allegation that the company was organized under the laws of New York is not an allegation that it is a corporation; in fact, the allegation is that the company is not a corporation, but a joint-stock company—that is, a mere partnership. And, although it may be authorized by the laws of the state of New York to bring suit in the name of its president, that fact cannot give the company power, by that name, to sue in a federal court."

A similar question was presented in the case of *Great Southern Fire Proof Hotel Company v. Jones*, 177 U. S. 450, 20 Sup. Ct. 690, 44 L. ed. 482. The defendant there was a limited partnership organized under a statute of Pennsylvania, and clothed with many of the attributes of a corporation. In fact, those limited partnerships so nearly resemble a corporation that the Circuit Court of Appeals of the Sixth Circuit in *Andrews Brothers Company v. Youngstown Coke Co., Limited*, 86 Fed. 585, 30 C. C. A. 293, held them to be corporations for the purpose of conferring jurisdiction upon the federal courts. But the Supreme Court, in the case of *Great Southern Fire Proof Hotel Company v. Jones*, declined to accept this interpretation, and refused to extend the presumption that the stockholders of a corporation are citizens of the state under which it is organized, to cover such limited partnerships, and reversed the case, with directions to dismiss it for want of jurisdiction. The same rule is again enforced, upon a full review of the authorities, in *Thomas v. Board of Trustees*, 195 U. S. 207, 25 Sup. Ct. 24, 49 L. ed. 160. * * * It is therefore the duty of this court to reverse the judgment below, and direct that the suit be dismissed for want of jurisdiction, and it is so ordered.⁴

HIBBS v. BROWN.

1907. 190 N. Y. 167, 82 N. E. 1108.⁵

APPEAL from an order of the Appellate Division of the Supreme Court in the first judicial department, entered April 6, 1906, which reversed an order of the Appellate Term affirming a judgment in favor of plaintiff entered upon a decision of the Municipal Court of the city of New York and granted a new trial.

⁴ *Chapman v. Barney* (1889) 129 U. S. 677, 9 Sup. Ct. 426, 32 L. ed. 800; *Great Southern Fire Proof Hotel Co. v. Jones* (1900) 177 U. S. 449, 20 Sup. Ct. 690, 44 L. ed. 842; *Thomas v. Board of Trustees* (1904) 195 U. S. 207, 25 Sup. Ct. 24, 49 L. ed. 160; *Gregg v. Sanford* (1895) 65 Fed. 151, 12 C. C. A. 525, 28 U. S. App. 313, *Accord*. See also, note, 14 Harv. L. R. 222.—Eds.

⁵ Statement abridged; portions of opinions omitted.—Eds.

This is an action to replevy some coupons originally attached to a bond issued by the Adams Express Company and appellant's right to succeed turns on the question whether said bond and coupons were negotiable and acquired by respondents in due course for value.

The bond was issued by the express company in and under its association name, and was one of an issue of twelve millions of dollars, secured by a certain trust indenture conveying and pledging for its payment a large amount of securities and property. It bore interest coupons of the ordinary form payable to bearer, and, except for two clauses to be specifically referred to, may be assumed to have been in the usual form of a corporation negotiable bond payable to bearer or the registered holder. Of the clauses to be particularly noted, one which is especially important provides that "no person or future shareholder, officer, manager or trustee of the Express Company shall be personally liable as partner or otherwise in respect to this bond or the coupons pertaining thereto, but the same shall be payable solely out of the assets assigned and transferred to the said Trust Company or out of other assets of the Express Company." The other clause refers to the deed of trust for a statement of the rights of the bondholders and of the securities and property securing the payment of the bonds. Amongst the provisions of said trust indenture thus referred to and made controlling upon the bondholders are several relating to enforcement of the trust and collection of the bonds which are claimed to confer upon a certain proportion of the bondholders the right to waive default in and postpone payment of interest coupons.

Hiscock, J.— * * * And thus we come at once to the last proposition and to the interesting and important question upon which we differ, whether the bonds, of which the one here involved is one, were rendered non-negotiable because of the clause already quoted exempting members of the Adams Express Company from that personal liability thereon which would ordinarily attach to the individual members of a joint stock association. * * *

Was the general credit of the obligor pledged?

The Adams Express Company was the maker of the bonds. They were issued by it in its artificial, corporate-appearing name, under its common seal, by its authorized executive officers and for its benefit. They expressed the general promise and obligation of the company which thus issued them, and were a claim against it upon which, as we shall see hereafter, judgment might be obtained or a receiver be appointed of it, and satisfaction obtained out of any or all of its joint, business, well-understood assets and property, and which we know aggregated many millions of dollars. Payment was not limited to the pledged securities or to any other part or parcel of the property of the association which made the bonds, but was a charge against the whole thereof. Thus far, therefore, they were entirely similar to the familiar bonds issued by an ordinary corporation which are general claims against it, and which are concededly

negotiable. But here it is that we come against the contention that this view of the character of the bonds however practical and desirable cannot prevail; that the exemption of the personal liability of the individual members of the association after all works a limitation upon the pledging of the general credit of the company which issued the bonds, and turns all of its assets, from which their payment may be enforced, into a special, limited fund.

As the foundation for this contention much care has been devoted to pointing out the difference between a joint stock association and a corporation, and to emphasizing the fact that the former is in effect a partnership, and that the individual liability of its members is just as essential a characteristic as it is in the case of a partnership, and that, therefore, it may not be eliminated without materially affecting the contract of the association.

Of course there can be no doubt that a joint stock association differs from a corporation, or that in its original conception and ultimate analysis it is like a partnership in respect to the individual liability of its members. But, upon the other hand, so many of the attributes and characteristics of a corporation have been impressed upon the modern joint stock association that in my opinion, for the purposes of the question now before us, we are amply justified in regarding simply the joint, *quasi* corporate, entity, and in saying that an obligation issued in its name upon its general credit, and binding all of its assets, complies with the requirements for a negotiable instrument, even though the practically unimportant individual liability of members is excluded.

We may briefly refer to some of these characteristics which, as I think, have led both courts and laymen to regard joint stock associations largely as corporate creations, and in ordinary business dealings quite to ignore the feature of individual membership and liability, even though it does exist. They are, like corporations, organized under and regulated by statutes (Laws 1894, chapter 235). They have, and transact business under, an artificial name. Their capital and ownership is represented by shares of stock transferable at will, and their existence is not dissolved or affected by the death of or transfer of interest by members. They have regular officers in whose names actions may be commenced in behalf of and against the association, and upon a judgment rendered in the latter case, execution may be issued only against property belonging to the association or to all of its members jointly. Formerly action could not be brought against the individual members of the association until after judgment and execution unsatisfied against the association. Now, although an action may be brought in the first instance against the members, still if the claimant elects to bring suit against the association he must then as formerly proceed to judgment and execution unsatisfied before instituting other suit against the members. And, as illustrating the complete and separate existence of the asso-

ciation as between it and the individual members, suit may be brought by it against such members. (Code, §§ 1919-1924.)

Based upon such statutory provisions decisions have been made and opinions written emphasizing their corporate characters as distinguished from the ordinary partnership wherein the individual relationship and liability of the members is universally recognized and of importance.

In *Waterbury v. Merchants' Union Express Co.* (50 Barb. 157), a case often cited, it was held that a receiver might be appointed of one of them, and it was said with reference to the powers conferred upon them by various statutes: "These are all attributes of a corporation, and if we look into the books for elementary definitions we shall find that corporations have not other attributes except the technical one of a common seal to distinguish them from common law partnerships. On the other hand, simple partnerships have none of the attributes or qualities here mentioned. * * * Looking at the substance and nature of things it is plain that in respect to the absence of a common seal merely these joint stock associations are like partnerships. In the other and vastly more material respects mentioned they are like corporations, although they are not declared to be such by the legislative acts referred to."

In *Matter of Jones* (172 N. Y. 575) it was held that shares in a joint stock association constituted personal property and were subject to the transfer tax irrespective of the character of the property represented thereby, whether real or personal. The court quoted with approval the statement in *Beach* in his work on *Private Corporations* (Vol. I, § 167) that "The powers conferred upon them by these enactments are such that for many purposes they are held to be corporations, even though they have nowhere been designated as such."

In *People ex rel. Platt v. Wemple* (117 N. Y. 136), it was held that the franchise or business of the United States Express Company, a joint stock association, was subject to taxation under certain statutes invoked for that purpose. The court, after referring to the powers and characteristics of the company not unlike those possessed by the Adams Express Company, says: "It seems obvious from these articles, that the arrangement consummated by them has little in common with a private partnership, for they provide for a permanent investment of capital, the right of succession, the transfer of property by an assignment of the certificate of ownership, and the prosecution of suits in the name of one person. The company has, therefore, the characteristics of a corporation, and, so far as it can it assumes to itself an independent personality and asserts powers and claims privileges not possessed by individuals or partnerships."

In *People ex rel. Winchester v. Coleman* (133 N. Y. 279), which was a proceeding by certiorari to review the action of taxing officials in imposing an assessment upon the capital stock of the National Express Company, a joint stock association, it was said: "It is then asserted that a series of statutes, beginning with the act of

1849, has ended in the gift to joint stock associations of every essential attribute possessed by and characteristic of corporations; * * * that the lines of distinction between the two, however far apart in the beginning, have steadily converged until they have melted into each other and become identical; that every distinguishing mark and characteristic has been obliterated, and no reason remains why joint stock associations should not be in all respects treated and regarded as corporations. Some of this contention is true. The case of *People ex rel. Platt v. Wemple* (117 N. Y. 136), shows very forcibly how almost the full measure of corporate attributes has, by legislative enactment, been bestowed upon joint stock associations until the difference, if there be one, is obscure, elusive and difficult to see and describe. * * * The two are alike but not the same. More or less, they crowd upon and overlap each other, but without losing their identity, and so, while we cannot say that the joint stock company is a corporation, we can say as we did say in *Van Aernam v. Bleistein* (102 N. Y. 360), that a joint stock company is a partnership with some of the powers of a corporation."

In *Oliver v. Liverpool, etc., Fire Ins. Co.*, (100 Mass. 531), it was held that an English joint stock association was subject to a tax assessable against "each fire * * * insurance company incorporated or associated under the laws of any government or state other than one of the United States." While there may be some slight difference between such a joint stock association and one existing under the laws of this state, what was said by the court is applicable to either. This statement was that "'joint stock companies are not pure partnerships, for their members are recognized as an aggregate body; nor are they pure corporations, for their members are more or less liable to contribute to the debts of the collective whole. They are associations of persons intermediate between corporations known to the common law and ordinary partnerships, and partake of the nature of both.' * * * And we are all of opinion that when, by legislative authority or sanction, an association is formed capable of acting independently of the rules and principles that govern a simple partnership, it is so far clothed with corporate power that it may be treated for the purposes of taxation as an artificial body."

In *State ex rel. R. & W. Comm. v. Adams Express Co.* (66 Minn. 271), it was held that the present joint stock association was so similar in many of its features to a corporation that it would be subject to the provisions of a statute providing for service of process upon a corporation.

Now while it is true that these statutes conferring upon joint stock associations the attributes of corporations, and the opinions discussing the similitude of the former to the latter do not destroy the element of individual liability, they do irresistibly force upon us appreciation of the fact that a great association like the Adams Express Company is very unlike an ordinary co-partnership and that it has assumed for ordinary, practical purposes in its business and

contractual relations the features and characteristics of a corporate creation, whereby the joint aggregate entity has been made prominent, and the individual units composing it have been overshadowed and obscured. Amongst other things, as we have seen, this organization in its aggregate capacity and under its artificial name which bears no relation to the identity of its members, may not only hold property, transact business and make contracts, but what is especially pertinent in this controversy those contracts may be enforced by proceedings against it which are entirely independent of any liability of individual members. In short, I do not think that we should transgress any proper limits, if we assumed that the public in dealing with the present bonds did so solely upon the faith and credit of the association, the entity which issued them, and without knowledge or thought of the individuals who composed it or their financial responsibility.

Under such circumstances we ought not to sacrifice substance to form and destroy the negotiable character of the bonds because of the exemption of individual liability unless we are compelled to, either by some controlling principle or authority, and, as I believe, there is neither which commands such a course. * * *

The order appealed from should be affirmed and judgment absolute rendered against appellant upon his stipulation, with costs.

O'BRIEN, J.—The only question in the case as to which there is any serious dispute is, as I conceive, whether the clause on the face of the bonds which provides that "no present or future shareholder, officer, manager or trustee of the Express Company shall be personally liable as partner or otherwise in respect of these bonds or the coupons appertaining thereto" deprives them of the character of negotiable paper. The contention of the plaintiff is that this clause destroys the negotiable quality of the bonds though payable to the bearer or holder. This clause contains also the statement that the bonds "shall be paid solely out of the assets assigned and transferred to the said trust company or out of the other assets of the Express Company." So that all the property of the company issuing the bonds was and is available to the holders as the source of payment and satisfaction thereof. I do not think that the obligations of a joint stock company payable to bearer are rendered non-negotiable from the fact that the paper upon its face contains a clause which exempts the shareholders and officers from liability so long as the general assets of the company are pledged for payment. But this is the disputed question in the case, and the contrary view is supported by an argument which rests mainly, if not entirely, upon the proposition that joint stock associations are partnerships, and that the obligations in question are the obligations of the individual shareholders, and that they are liable upon them, jointly and severally, the same as partners. Stating the argument in another way it comes to this: The bonds in this case are the bonds of a partnership, made in the name of the firm, and though containing a promise to pay the bearer or holder

a specified sum of money in the future, upon a day certain, yet the promise is coupled with a condition that none of the partners shall ever be held liable. If the premises upon which the argument is based are correct, it would, I admit, be difficult to resist the conclusion; unless, indeed, it could be held that the conditions might be rejected as utterly inconsistent with and repugnant to the promise and, therefore, void. Adopting the theory that the bonds are the obligations of the shareholders as partners, the repugnancy is quite obvious. But I do not think that the bonds in question are in any proper or legal sense partnership obligations made by the shareholders as partners. Primarily the promise to pay the bearer or holder is not the promise of the shareholders, but of the legal entity represented by the express company as such.

A joint stock company, whatever else may be said about it, is certainly for most, if not all practical purposes, a legal entity capable in law of acting and assuming legal obligations quite independent of the shareholders. The idea that these companies occupy some undefined and undefinable ground midway between a partnership and a corporation has practically faded away and cannot be applied to the question with which we are now concerned. It is not very important to inquire what they were in their origin, but rather what they are now, or at least were when the bonds in question were issued and sold to the public. It seems to be conceded or assumed that if the express company, at the time of issuing the bonds, had been incorporated by filing the usual certificate for that purpose, the clause exempting the shareholders from liability would not affect their negotiable character. It remains only to consider what sound distinction, if any, can be made between the twelve millions of bonds issued by the express company and the other untold millions of other bonds issued by corporations. They are all negotiable in form, that is to say, payable to order or bearer, as the case may be. Assuming that the shareholders of a corporation are or may be liable for the corporate debts, and that the clause referred to would not affect the negotiable quality of its paper, what reason is there for holding that the clause destroys the negotiable quality of the bonds in question? The proposition that in the one case the bonds import a promise to pay by a corporate body and in the other the promise of individuals as partners or as a partnership firm, does not seem to me to be reasonable or tenable. The argument in support of that theory would seem to be somewhat strained. The general rules of law that govern partnerships have very little application to joint stock companies, at least so far as concerns the question now under consideration. The principle of agency which enables one partner to bind all his associates as well as the firm has no application to such companies. The death of one or more of the members of the company does not work a dissolution. The doctrine of survivorship, so important as between partners, does not exist as to such companies, and so it would be difficult to state a single general rule of partnership law that in its full extent could be applied to such companies.

On the other hand, there are very few of the legal principles that apply to corporations that do not apply in some form to these companies. They are taxed and perpetuated through the shares of stock as corporations are. They are entitled to assume an artificial name, to sue and are subject to be sued. They may use a common seal and through the shares of stock they have perpetual life even in a larger sense than corporations have. Their general powers and duties to the public are practically the same and regulated in the same way as corporations. I need not pursue the comparison any further, nor enlarge upon it, since the learned opinion of my associate, Judge Hiscock, who has referred to the various judicial views on the subject, pro and con, fully covers that feature of the case.

It is very true that the shareholders of such companies are liable ultimately for the company's obligations, but that does not make such companies partnerships in the sense that their obligations are the contracts or promises of the shareholders. The shareholders of corporations are or may be liable in the same way, but such liability is not, of course, that of partners. The statutes of this state prescribing the method of procedure in suits by and against joint stock companies (Code Civ. Proc., §§ 1919 to 1924) do not qualify what has been stated concerning the legal nature of such companies. They embody the distinct idea that the liability of the shareholders is not primary, but secondary, the same as in case of corporations; and even if these statutes had never been enacted it is quite likely that the Adams Express Company could, in that artificial name, sue and be sued in the same manner as a corporation, since the State Constitution (Art. 8, § 3), while enacting that corporations have the right to sue and are subject to be sued the same as natural persons, defines joint stock companies having any of the powers and privileges not possessed by individuals or partnerships as corporations within the meaning of that section. The main purpose of these provisions of the code would seem to be the enactment of a mode of procedure which would enable creditors of the company, or parties having a cause of action against it, to exhaust all legal remedies against the company as a legal entity before resorting to the personal liability of the shareholders analogous to similar rules applicable to corporations. It is, I think, very difficult to avoid the conclusion that these companies at this day and in this state possess substantially and practically all the attributes of corporations, and still more difficult to assign any sound reason for any distinction to be made between the negotiable character of the bonds of each when made payable to bearer. These companies are for all practical purposes *quasi* corporations, and it seems to me are clearly such so far as concerns the negotiable character of its commercial paper or promise to pay a specific sum of money to bearer upon a day certain.

If the bonds in their present form had been stolen from the Adams Express Company by one of its clerks or employes, or even a stranger, and they had been put in circulation and passed from hand to hand to the possession of an innocent holder who had purchased

eral tenor of the bonds which are intended to be negotiable and which have been purchased by the public as such and, therefore, should be eliminated and disregarded. Still further, I agree with the opinion of Judge Edward T. Bartlett that any provision in the contract of a joint stock association relieving the shareholders from liability is contrary to public policy and void, since it would enable the shareholders of such associations to obtain all the immunities of stockholders in a corporation without incorporating and subjecting themselves to the restrictions and regulations imposed by law on corporations.

WERNER, J.— * * * The bonds of this issue are payable solely out of the assets assigned and transferred to the trustee or out of the other assets of the express company. If the express company were a corporation this would clearly be an unconditional promise for it would be a general pledge of the credit of the maker; a tender of all it had to give in satisfaction of the debt. But the company is concededly not a corporation, although our statutes have invested it with certain corporate attributes. It is unnecessary to enumerate these since it cannot be disputed that in respect of the individual liability of the shareholders of a joint stock company for the company debts, the common-law rule still obtains. Each shareholder is liable precisely as though he were a member of an unlimited partnership. (*Townsend v. Goewey*, 19 Wend. 424; *Dennis v. Kennedy*, 19 Barb. 517; *Wells v. Gates*, 18 id. 554; *Cross v. Jackson*, 5 Hill, 478.) Although, as we have stated, joint stock companies have been granted certain privileges and immunities peculiar to corporations, this most distinctive difference between these corporate and non-corporate creatures of the law has been consistently preserved by the legislature and recognized by the courts. (Code Civ. Pro., §§ 1919-1924; *People ex rel. Winchester v. Coleman*, 133 N. Y. 279; *Van Aernam v. Bleistein*, 102 N. Y. 360; *Matter of Jones*, 172 N. Y. 575.)

From what has been said it must follow that if the clause in the bonds exempting the individual shareholders of the express company from liability is valid, the bonds are non-negotiable, because they are in effect, if not explicit terms, made payable out of a particular fund, so that the promise to pay is not unconditional. The clause under discussion is the only substantial thing that differentiates these bonds from the ordinary corporate bonds which are issued and held by the millions and are recognized and classed as negotiable instruments. The maker of the bonds is an association having a business name, which it used in making them, having shares of capital stock, indefinite succession, and a number of other characteristics which the lay public associates exclusively with corporations. These considerations lend great force to the suggestion that as a matter of public policy the exemption clause referred to should be treated as nugatory, so that the bonds may be invested with that element of negotiability which may fairly be regarded as one of the principal items of their value, and one of the most important inducements to their

current sale and purchase. I deem it unnecessary to go quite so far as that in the case at bar, since I am convinced that the exemption clause is so repugnant to the terms, tenor and purpose of the bonds that it not only may but must be taken out of the instruments in order to preserve their negotiability and even their validity. It would be rather difficult to explain upon what theory the obligation of these bonds could be enforced in an action at law if the exemption clause is retained as a part of the bond. The maker cannot be sued in its business name, and the officers which represent it can only be sued upon obligations for which an action could be maintained against all the stockholders. (Code Civ. Pro. § 1919.) We are presented, in short, with the legal paradox that a written obligation, obviously intended to be negotiable, cannot be enforced in a court of law. This is an anomalous condition so utterly at variance with the manifest purpose of the association in issuing these bonds, and so palpably destructive of the legal rights of the holders thereof, that we could hardly give the exemption clause the effect which its language imports without destroying the validity of the bonds themselves.

Since both the negotiability and the validity of the bonds may be secured by the abrogation of the exemption clause, and since there is nothing in the terms of the instruments to prevent this manifestly just disposition of the case, I conclude this branch of the discussion with the recommendation that the exemption clause be held void, and that the bonds and coupons be held negotiable. Upon the other questions I agree with the majority.

Holding these views, I think there should be an affirmance of the order of the Appellate Division, and that judgment absolute should be rendered against the appellant with costs, in accordance with his stipulation.

GRAY and HAIGHT, JJ., concur with HISCOCK, J.; O'BRIEN, J., concurs with HISCOCK, J., in opinion; CULLEN, Ch. J., concurs in result in memorandum; EDWARD T. BARTLETT and WERNER, JJ., read opinions concurring in result.

*Ordered accordingly.**

* See N. Y. Const. Art. VIII, sec. 3; N. Y. Joint Stock Ass'n Law, chap. 45; N. Y. Code Civ. Proc., secs. 1919, 1920, 1923; N. Y. Stat. Const. Law, sec. 5. Cf. *McMahon v. Raube* (1871) 47 N. Y. 67; *McCabe v. Goodfellow* (1892) 133 N. Y. 89, 30 N. E. 728; *People v. Coleman* (1892) 133 N. Y. 279, 31 N. E. 96; *Jones' Estate* (1902) 172 N. Y. 575, 65 N. E. 570; *Lane v. Albertson* (1903) 78 App. Div. (N. Y.) 607, 79 N. Y. S. 947.

In *Eliot v. Freeman* (1910) 220 U. S. 178, 31 Sup. Ct. 360, 55 L. ed. 424, Day, J., discussing the Federal Corporation Tax Law of Aug. 5, 1909, said: " * * * the tax is imposed upon doing business in a corporate or quasi-corporate capacity, that is, with the facility or advantage of corporate organization. It was the purpose of the act to treat corporations and joint-stock companies, similarly organized, in the same way, and assess them upon the facility in doing business which is substantially the same in both forms of organization."—Eds.

Section 5.—Considered in Relation to its Members. The Distinction Between Capital Stock and Shares of Stock.

BLIGH v. BRENT.

1837. 2 Y. & C. Ex. 268.¹

ALDERSON, B., delivered the judgment of the court: This was a bill praying in substance that the defendant Margaret Brent, widow and executrix of Timothy Brent, deceased, may account for certain shares of the Chelsea Waterworks, and that it may be declared by the court that the plaintiff as his heir at law became entitled to those shares, and that the other defendants, the governor and company of the Chelsea Waterworks, may be directed to insert in their transfer-books the plaintiff's name as proprietor thereof. There is no dispute as to the facts, and the only question for the court was, whether these shares were part of the real or personal estate of the testator. If the former, the plaintiff as heir at law is entitled to the decree he prays, because the will is attested by only two witnesses; and if the latter, his bill must be dismissed. * * *

The company of the Chelsea Waterworks was originally constituted under the provisions of the statute 8 Geo. I, 1723. By that act, certain persons named therein were constituted commissioners, undertakers, and trustees for carrying into effect the works then projected, and for afterwards maintaining them. For that purpose his Majesty was, by a subsequent clause, empowered to incorporate them, by the name of the Governor and Company of the Chelsea Waterworks. And they were to have the power of purchasing lands not exceeding £1,000 per annum, and to sell and dispose thereof at their pleasure, and to do all necessary works, and to be subject to such rules, qualifications, and appointments as his Majesty should think reasonable to be inserted in the charter; and might also be empowered to make by-laws from time to time for the good government of the corporation.

In pursuance of this power a charter of incorporation was granted almost immediately afterwards by George I. That charter followed the directions of the statute, and gave the corporation power to purchase lands, etc., so as they did not exceed in value £1,000 per annum, and also estates for life or lives, and for years, and goods and chattels of what nature or value soever, for the better carrying on and effecting the purposes of the company, not exceeding the value of the joint stock of the corporation thereafter mentioned and limited, and to be taken and computed as part thereof.

The twenty-third section empowered the corporation by subscription to raise a joint stock, not exceeding £40,000, and to manage the same from time to time, and to receive the benefit and advantage of

¹ The facts are sufficiently stated in the opinion.—Eds.

the same to the use of them the said Governor and Company and their successors, according to such shares and proportions as they or any of them have or shall have therein. And then it provided that every person subscribing and contributing any sum or sums of money should, by virtue thereof, become members of the said corporation, and should be entitled to a share or shares in such joint stock (previously fixed at £20 each) equal to the sum or sums of money so by him actually contributed and paid in, and no greater; and should be enabled to sell, assign, and transfer the same or any part thereof (not being less than one whole share, as by a subsequent clause was provided), by transfers in the company's books, in such manner as should be by a general court directed, or by his last will and testament; and the person to whom such assignment or transfer, or disposition by last will and testament, should be made, should by virtue thereof become member of the said corporation.

What, then, is the intention of the crown and legislature to be collected from all these particulars as to the nature of the interest which each shareholder is to have? That is, in truth, the whole question in this cause. Now, in the first place, we have a corporation to whose management the joint stock of money subscribed by its individual corporators is intrusted. They have power of vesting it at their pleasure in real estate or in personal estate, limited only as to amount, and of altering from time to time the species of property which they may choose to hold; and in order to give them greater facilities and advantages, certain powers are intrusted to the undertakers by the legislature, and that even before they were constituted a body corporate, of laying down pipes, and thereby occupying land for the purposes of their undertaking. These powers render the use of joint stock by the body corporate more profitable, but they form no part of the joint stock itself; and one decided test of this is, that they belong inalienably to the corporation, whereas all the joint stock is capable expressly of being sold, exchanged, varied, or disposed of at the pleasure of the corporate body. It is of the greatest importance to look carefully at the nature of the property originally intrusted, and that of the body to whose management it is intrusted,—the powers that body has over it, and the purposes for which these powers are given. (The property is money,—the subscriptions of individual corporators.) In order to make that profitable, it is intrusted to a corporation who have an unlimited power of converting part of it into land, part into goods, and of changing and disposing of each from time to time; and the purpose of all this is the obtaining a clear surplus profit from the use and disposal of this capital for the individual contributors.

It is this surplus profit alone which is divisible among the individual corporators. The land or the chattels are only the instruments—and those varying and temporary instruments—whereby the joint stock of money is made to produce profit. Suppose the subscription had not been by the individual corporators, but that stran-

gers, having collected the money, had put it into the management of a corporate body having particular privileges, and had, after giving them power to vest the money at their pleasure, stipulated to receive these profits: could it be contended that the nature of the property of the subscribers depended on the mode of management by the independent body? And yet that is, in truth, this case; for the individual members of a corporation are quite as distinct from the metaphysical body called "the corporation," as any others of his Majesty's subjects are. (The learned judge then distinguished several earlier cases.) But here the case is wholly different,—the property intrusted is money; the corporation may do what they like with it, and may obtain their profit in any way they please from the employment of their capital stock. If they thought that they could with greater profit supply water by conveying it in carts or the like, they would have a perfect right so to do. It would be strange that the nature of these shares should continually fluctuate, and be sometimes real estate, and sometimes personal, according as the corporation in the course of their management should choose to hold real or personal property. Suppose a man made his will, attested by two persons, and at a time when the corporation held only personal estate. It is good. He becomes lunatic or is incapable from age, and then real property is bought by the corporation. Is his will to be set aside? And yet he cannot make another.

Then, in what way has this property always been treated? If we look to the wording of the charter, the language is much more suitable to personal than to real estate. Indeed, on the latter supposition it is very inaccurate. Again, the form of transfer appointed by the legislature (for that which is done under the provisions of the charter is, in fact, done by the legislature, and is, indeed, subsequently recognized by it) is applicable to personal estate only. These shares are not transferred to A. B. and his heirs, but A. B., his executors, administrators, and assigns; and so they have always been. This form, indeed, may be considered as almost a contemporary exposition of the law on this point.

Lastly, in *Weekley v. Weekley*, this point came expressly under the consideration of Sir Thomas Sewell, master of the rolls, and he decided that these shares were personal property.

Upon the whole, therefore, we think that the principles of law, the usage of the company, and the distinct authority of one decided case are sufficient to warrant us in coming to the conclusion that these shares are personal property.

*Bill dismissed.*²

² *South-Western R. Co. v. Thomason* (1869) 40 Ga. 408; *First National Bank v. Smith* (1872) 65 Ill. 44; *Russell v. Temple* (1798) 3 Dane's Abr. (Mass.) 108; *Johns v. Johns* (1853) 1 Oh. St. 350; *Tappan v. Merchants' Nat. Bank* (1873) 19 Wall. (U. S.) 490, 22 L. ed. 189, *Accord.* *Welles v. Cowles* (1818) 2 Conn. 567; *Hurst v. Meason* (1835) 4 Watts (Pa.) 346; *Price v. Price's Heirs* (1836) 6 Dana (Ky.) 107, *contra*, are no longer law.

COMMONWEALTH v. NEW YORK & C. R. Co. (1890) 132 Pa. St. 591, 19 Atl.

PEOPLE v. COLEMAN.

1891. 126 N. Y. 433, 27 N. E. 818.*

FINCH, J.—The relator has been assessed upon an “actual value” of its capital stock derived entirely from the market value of its shares. These are selling at the large premium of something over five hundred dollars for each share of one hundred dollars, and the assessors have concededly taken that valuation, or the principal part thereof, as the “actual value” of the company’s stock liable to taxation, instead of its own proved and established value. The relator challenges the assessment, and through all the proceeding has persistently raised and pressed the inquiry, not so much as to the mode or manner of ascertaining value, but rather as to what is the precise thing to be valued, whether the capital stock of the company or the capital stock held in shares by the corporators. If these are the same, or, in any just sense, equivalents, either might be valued without substantial error, but if they are not such, we must determine which is to be valued before we can solve the problem of how to value it.

Now, it is certain that the two things are neither identical nor equivalents. The capital stock of a company is one thing; that of the shareholders is another and different thing. That of the company is simply its capital, existing in money or property, or both; while that of the shareholders is representative, not merely of that existing and tangible capital, but also of surplus, of dividend earning

291. This was an action by the state of Pennsylvania against the Railway Co., a New York corporation, to escheat certain lands in Pennsylvania. A statute of Pennsylvania provided that no foreign corporation should hold any real estate directly in the corporate name, or by or through any trustee or other device whatsoever, unless specially authorized. *Held*, that the defendant corporation, which held all the stock of a Pennsylvania corporation which owned the land in question, did not come within the terms of the statute. See also *Durant v. Kennett* (1869) L. R. 5 C. P. 262; *United States v. Wolters* (1891) 46 Fed. 509.

FOSTER & SONS, LIMITED v. COMMISSIONERS OF INLAND REVENUE (1894) L. R. 1 Q. B. 516. *Held*, that a transfer of property by the owners thereof to a corporation composed of the owners was subject to a stamp tax imposing a tax on every “conveyance or sale.” Lindley, L. J.—“Again it is argued on behalf of the appellants that this instrument is in substance nothing more than a conveyance to a trustee to carry on the business in trust for the grantor. Just try that. Supposing there is a conveyance by half-a-dozen people, transferring their property to a trustee on trust to carry on the business for them, can you in any sense of the word, legal or business-like, or otherwise, call that trustee a buyer? There is no buying, there is no sale to him at all, nor is there any money, or stock, or securities, or anything else parted with by him.” (p. 529).

In *Gallagher v. Germania Brewing Co.* (1893) 53 Minn. 214, Mitchell, J., said: “The facts of the present case appeal to a natural sense of justice, for while, by fiction of law, a corporation is a distinct entity, yet in reality it is an association of persons who are in fact the beneficial owners of all the corporate property.” (p. 218).—Eds.

*The facts sufficiently appear in the opinion. Portion of opinion omitted.—Eds.

power, of franchise and the good will of an established and prosperous business. ¶ The capital stock of the company is owned and held by the company in its corporate character; the capital stock of the shareholders they own and hold in different proportions as individuals. ¶ The one belongs to the corporation; the other to the corporators. ¶ The franchise of the company, which may be deemed its business opportunity and capacity, is the property of the corporation, but constitutes no part or element of its capital stock; while the same franchise does enter into and form part, and a very essential part, of the shareholder's capital stock. While the nominal or par value of the capital stock and of the share stock are the same, the actual value is often widely different. The capital stock of the company may be wholly in cash or in property, or both, which may be counted and valued. It may have in addition a surplus, consisting of some accumulated and reserved fund, or of undivided profits, or both, but that surplus is no part of the company's capital stock, and, therefore, is not itself capital stock. The capital cannot be divided and distributed; the surplus may be. But that surplus does enter into and form part of the share stock, for that represents and absorbs into its own value surplus as well as capital, and the franchise in addition. So that the property of every company may consist of three separate and distinct things, which are its capital stock, its surplus, its franchise; but these three things, several in the ownership of the company are united in the ownership of the shareholders. The share stock covers, embraces, represents all three in their totality, for it is a business photograph of all the corporate possessions and possibilities. A company also may have no surplus, but, on the contrary, a deficiency which works an impairment of its capital stock. Its actual value is then less than its nominal or par value, while yet the share stock, strengthened by hope of the future and the support of earnings, may be worth its par, or even more. And thus the two things—the company's capital stock and the shareholder's capital stock—are essentially and in every material respect different. They differ in their character, in their elements, in their ownership and in their values. How important and vital the difference is, became evident in the effort by the state authorities to tax the property of the national banks. The effort failed, and yet the share stock in the ownership of individuals was held to be taxable as against them. The corporation and its property were shielded, but the shareholders and their property were taxed.

Now some degree of confusion and trouble have come in because these two different things are denominated alike capital stock, making the expression sometimes ambiguous. It is the important and decisive phrase in the law of 1857, under which the assessment here resisted was made, and requires of us to determine at the outset in which sense it was used. The section reads thus: "The capital stock of every company liable to taxation, except such part of it as shall have been excepted in the assessment-roll, or shall have been exempted by law, together with its surplus profits or reserved funds

exceeding ten per cent. of its capital, after deducting the assessed value of its real estate, and all shares of stock in other corporations actually owned by such company which are taxable upon their capital stock under the laws of this state, shall be assessed at its actual value and taxed in the same manner as the other real and personal estate of the county."

There are reasons in abundance for the conclusion that by the phrase "capital stock" the statute means not the share stock, but the capital owned by the corporation; the fund required to be paid in and kept intact as the basis of the business enterprise, and the chief factor in its safety. One ample reason is derived from the fact that the tax is assessed against the corporation and upon its property, and not against the shareholders, and so upon their property. In theory every tax is charged against some person, natural or artificial, resident or non-resident, known or unknown. It is assessed not upon property irrespective of ownership, but against persons in respect to their property (23 N. Y. 215), and effects not merely a lien, but also a personal liability. On the assessment-rolls in this case appeared the name of the relator as the person assessed, and the amount of the tax became a charge against it. Of course, it could only be assessed and taxed in respect to its own property, that which in its corporate character it owned and possessed, and so it follows inevitably that the statute concerns the company's capital stock, that is its real and actual capital, and not in any respect the share stock which it does not own and whose possessors have not been assessed.

Another reason is found in those terms of the statute which include and exclude respectively specific kinds or classes of property in the corporate ownership. Thus the assessment is to be laid not merely upon the capital stock of the corporation, but also upon its surplus. No such explicit direction was necessary, except upon the assumption that by the words "capital stock" was meant simply "capital," which would not include surplus, and so required that it be subjected by name to the valuation. If the share stock was meant its value would include surplus and make its specification not only needless but confusing. But while the statute includes surplus by specific mention, it excludes franchise by omitting it. The omission of franchise is emphasized by the careful inclusion of surplus. It is fully and definitely settled that the tax imposed by the statute is not upon franchise. (*People v. Comrs. of Taxes*, 2 Black's (U. S.) 620.) But if that be so, it is not upon the share stock, for that represents the value of the corporate franchise as a part of the total of the corporate property. And so, both by what it specifically includes and silently excludes, the statute itself informs us that by "capital stock" it means and intends the company's actual capital paid in and possessed, and not at all or in any sense the share stock.

The same thing becomes apparent from a study of the whole line of legislation which culminated in the law of 1857. It was traced in detail upon the argument with great industry and wealth of illustration. We have verified it by traveling over the same track, and with-

out taking pains to reproduce it, may assert the general result which it discloses and select out one or more illustrations. The investigation shows that the word "capital" and the phrase "capital stock" are used interchangeably and synonymously, and where the latter phrase occurs there is almost always something in the statute which stamps and labels it as referring to the actual capital of the company. Thus the law of 1825 (Chap. 262), after providing for the taxation of all persons owning or possessing property, proceeds to declare that corporations shall be deemed persons for the purposes of the act, and requires them to furnish a statement of the amount of "capital" actually paid in; and then, referring to turnpike and bridge companies, requires them to state "the amount of capital stock actually paid in or secured to be paid in." Both clauses refer to the same assets or fund, naming it indiscriminately "capital" and "capital stock." Again, in the law of 1825 (Chap. 254) the assessors, after putting the corporation by name on the assessment-roll, are required to add the amount "of its capital stock paid in or secured to be paid in," and to designate how much of it is in real and how much in personal property, and so no doubt is left that by "capital stock" was meant simply the "capital" possessed in cash or invested in securities or real estate.

The illustrations might be multiplied and fortified by reference to numerous acts relating to the formation or management of manufacturing, railroad, business and telegraph companies in which the two forms of expression are used indiscriminately and as convertible terms; but I think quite enough has been said to require unhesitating assent to the proposition that under the law of 1857, the thing to be taxed is the capital of the company and not the shares of the stockholders.

Indeed, I should feel bound to apologize for arguing what seems to me so simple and plain a proposition, were it not for the fact that it has been largely ignored by assessors and not always clearly kept in mind by the courts, and but for the further fact that the right to adopt as the taxable valuation the value of the shares, totally disregarding the value of the company's capital, has been asserted in this case, maintained by the courts below, and claimed to be fully justified by very much which we ourselves have decided or said.

(The learned judge proceeded to examine the earlier cases in detail.)

And so I think the authorities either fairly permit or fully justify the conclusions which I have reached and which may be stated with reasonable accuracy thus: First, the subject of valuation and assessment is never the share stock, but always the company's capital and surplus.¹ Second, such capital and surplus must be assessed at its own value, and when that is correctly known and ascertained, no other value can be substituted for it.² Third, where its amount and value are undisclosed and unknown the assessors may consider the market value of the share stock and the general condition of the company as indicative of surplus or deficiency and of the probable amount

of either.¹ Fourth, they may further resort to such means of information when the amount of capital and surplus is disclosed, but the assessors have sufficient reason to disbelieve the statement, and such reason is founded upon facts established by competent proof.

If these conclusions are correct it will follow that the assessment complained of should be canceled. The corporation presented to the assessors a sworn statement of its assets and liabilities. If it be true, there was nothing subject to assessment. But its truth is not questioned, and there is not the least reason to doubt it. The assessors did not doubt it: they merely deemed it immaterial, and so testified when examined. In other words, knowing with certainty the value of one thing, they claimed the right to affix to it the larger value of a different thing. Authorized only to tax against the company its capital and surplus, they assumed the right practically to tax it for the share stock held by individuals. They have not in terms claimed that the share stock is the subject of taxation, nor has the counsel who represented them on the argument, but both have maintained and defended what is the exact and complete equivalent. The right asserted is a discretion in the assessors at their free will to assess corporations upon and at the value of their capital and surplus, or upon and at the value of the share stock independently of established facts and whenever they please. The law gives them no such discretion. How it has been exercised and how destructively to the rights of taxpayers may be seen by comparing the action in this case with that in one of the cases which we have reviewed. Where the share stock was selling at ninety, and so below par, the assessors refused to take that value and went to the company's books in search of a larger one, which they found and adopted. Here, where the actual value of capital and surplus is established so that they frankly admit the fact, they calmly disregard it and fly to the larger value of the share stock. The statute has given them no such right. They are not lawless rovers, wandering among corporations at will, but regular officers bound by discipline and controlled by the law, and whose discretion exists within fixed and definite limits. * * *

It follows that the judgment and order of the General and the Special Term should be reversed and the assessment against the relator vacated and canceled, without costs.

All concur, except PECKHAM, J., not voting.

*Judgment reversed.*⁴

¹Porter v. Rockford &c. R. Co. (1875) 76 Ill. 561; Danville &c. Trust Co. v. Parks (1878) 88 Ill. 170; People v. Morgan (1904) 178 N. Y. 433, 70 N. E. 967, *Accord*.

In Van Allen v. Assessors (1865) 3 Wall. (U. S.) 573, 18 L. ed. 229, *held*, that shares of stock of national banking corporations are subject to State taxation, though a part or the whole of their capital stock is invested in Federal securities declared by Congress to be "exempt from taxation by or under State authority."—Eds.

[NOTE. The relation between the corporation and its members should be further considered in connection with cases *infra*, Chap. 8.]

CHAPTER II.

CORPORATIONS DE JURE.

Section 1.—Under Special Acts or General Laws.

Co. Lit. 250 a. And this body politike, or incorporate, may commence, and be established three manner of ways, viz., by prescription, by letters patents, or by act of parliament.

1 Bl. Com., 474. The king, it is said, may grant to a subject the power of erecting corporations, though the contrary was formerly held; that is, he may permit the subject to name the person and powers of the corporation at his pleasure; but it is really the king that erects, and the subject is but the instrument: for though none but the king can make a corporation, yet *qui facit per alium, facit per se*. * * * In this manner the chancellor of the University of Oxford has power by charter to erect corporations; and has actually often exerted it.

STATE ON INFORMATION OF CARLTON v. DAWSON.

1864. 22 Ind. 272.

APPEAL from the Clark Circuit Court.

WORDEN, J.—This was an information against the appellees, charging them in substance, with usurping and exercising the powers and functions of a railroad corporation, under the pretended authority of an act of the legislature, entitled, "An act to Incorporate the Fort Wayne and Southern Railroad Company," approved *January* 15, 1849. It is alleged that the corporators named in the act did not accept the charter and franchises until *June*, 1852; that as there had been no acceptance of the charter up to November 1, 1851, the act was then repealed by the Constitution of the State, which then took effect.¹ Prayer for judgment of ouster.

Issue, trial, finding, and judgment for the defendants.

The case comes before us on the evidence.

In the case of *The State v. Dawson*, 16 Ind. 40, it was held that if the charter was not accepted by the corporators until the new consti-

¹ The Constitution (Art. 11, sec. 13) contained this provision: "Corporations, other than banking, shall not be created by special act, but may be formed under general laws." See *State v. Dawson* (1861) 16 Ind. 40.—Eds.

tution took effect, it was thereby repealed, and no valid organization could thereafter take place under the act. The question was there decided on demurrer. In the case before us, an issue of fact was made and tried; and the evidence shows, as we think, pretty conclusively, that the corporators named in the act did accept the charter before the new constitution took effect.

The act in question provides that *Allen Hamilton* and others, naming them, and their associates and successors in office, etc., "are hereby constituted a body corporate and politic, by the name and style of *The Fort Wayne and Southern Railroad Company*, and shall be able and capable in law to sue and be sued," etc.

It was not only proven that the corporators applied to the legislature for the passage of the act in question, already drawn up as passed, excepting the clause authorizing a repeal; that one of the corporators appeared before a legislative committee, to whom the bill was referred, and on behalf of himself and the other corporators, explained to the committee the objects of the proposed organization; but it was also proven that, after the legislature appended the clause authorizing a repeal in certain cases, such of the corporators as were present, one of whom, at least, appears to have been acting by the authority, express or implied, of those who were absent, met together and consulted upon the amendment, and agreed to accept the charter in that form. If the evidence stopped here, it would be clearly sufficient to show an acceptance. "If a peculiar charter is applied for, and it is given, there can be no reasonable ground to doubt of its immediate acceptance." Ang. & Ames on Corp., § 83.

But in addition to this, the evidence shows that in *October, 1851*, a meeting was held of a majority of the corporators named, when they determined to build the contemplated railroad, under the charter.

The corporators having accepted the charter before the constitution of 1851 took effect, it became a valid, binding contract between the State and the corporators, which could not be abrogated or impaired except for cause.

Per Curiam.—*The judgment below is affirmed.*²

² *Rutter v. Chapman* (1841) 8 M. & W. 1, esp. p. 17; *City of Atlanta v. Gate City &c. Co.* (1883) 71 Ga. 106; *Harriman v. Southam* (1861) 16 Ind. 190; *Gillespie v. Fort Wayne R. Co.* (1861) 17 Ind. 243; *Taylor v. Newberne* (1885) 55 N. C. (2 Jones Eq.) 141, esp. 146-7, *Accord*.

"It has long been the received opinion that there must be an acceptance, but the mode of proving it has always been left open. In general, the acceptance of a charter has been proven by evidence of acting under it." Lord Tenterden, C. J., in *R. v. Hughes* (1827) 7 B. & C. 708, at p. 718. See *Perkins v. Sanders* (1879) 56 Miss. 733; *St. Joseph &c. R. Co. v. Shambaugh* (1891) 106 Mo. 557, *Accord*.

"The acceptance must not only be within reasonable time, but it must be of that which is offered." *Irving, J.*, in *Bonaparte v. Baltimore &c. R. Co.* (1892) 75 Md. 340.

Acceptance at a meeting held without the state granting the charter is invalid. *Smith v. Silver Valley Min. Co.* (1885) 64 Md. 85. Cf. *Heath v. Silverthorn &c. Co.* (1875) 39 Wis. 146.—Eds.

FRANKLIN BRIDGE CO. v. WOOD.

1853. 14 Ga. 80.

ASSUMPSIT in Heard Superior Court.

The Franklin Bridge Company was incorporated under the Act of the Legislature of 1843, to prescribe the mode of incorporating companies for certain purposes, by an order of the Inferior Court of Heard County.

The company sued the defendant, Wood, for his subscription to their stock.

The defendant pleaded that the company was not legally incorporated; contending that the act of the Legislature referred to, was unconstitutional and void.

Upon argument, the court held that the act aforesaid was unconstitutional, and nonsuited the plaintiffs.

To this decision plaintiff excepted.

LUMPKIN, J.—Is the Act of 1843 and that of 1845, amendatory thereof, pointing out the manner of creating certain corporations and defining their rights, privileges, and liabilities, unconstitutional?

By the first section of the Act of 1843, it is provided "That when the persons interested shall desire to have any church, camp-ground, manufacturing company, trading company, ice company, fire company, theatre company, or hotel company, bridge company, and ferry company, incorporated, they shall petition in writing the Superior or Inferior Court of the county where such association may have been formed, or may desire to transact business for that purpose, setting forth the object of their association, and the privilege they desire to exercise, together with the name and style by which they desire to be incorporated; and said court *shall pass a rule or order*, directing said petition to be entered of record on the minutes of said court."

Section 2 enacts "That when such rule or order is passed, and said petition is entered of record, the said companies or associations shall have power respectively, under and by the name designated in their petition, to have and use a common seal; to contract and be contracted with; to sue and be sued; to answer and be answered unto in any court of law or equity; to appoint such officers as they may deem necessary; and to make such rules and regulations as they may think proper for their own government; not contrary to the laws of this State; but shall make no contracts or purchase or hold any property of any kind, except such as may be absolutely necessary to carry into effect the object of their incorporation. Nothing herein contained shall be so construed as to confer banking or insurance privileges on any company or association herein enumerated; and the individual members of such manufacturing, trading, theatre, ice, and hotel companies, shall be bound for the punctual payment of all the contracts of said companies, as in case of partnership."

The third section declares that "No company or association shall

be incorporated under this act, for a longer period than fourteen years; but the same may be renewed whenever necessary, according to the provisions of the first section of this act."

The fourth section confers upon the Superior and Inferior Courts respectively, the power to change the names of individuals.

Section fifth. "For entering any of said petitions and orders, and furnishing a certified copy thereof, the clerk shall be entitled to a fee of five dollars; except in cases of applications by individuals for the change of names,—in which case, the clerk of said court shall be entitled to the fee of one dollar. And that such certified copy shall be evidence of the matters therein stated in any court of law and equity in this State." Cobb's Digest, 542, 543.

By the Act of 1845 the provisions of the Act of 1843 are extended to all associations and companies whatever, except banks and insurance companies; and the individual members of all such incorporations are made personally liable for all the contracts of said associations or companies. Ibid.

The argument against the validity of the charter of the Franklin Bridge Company, created under these statutes, is this:—

1. That in England, corporations are created and exist by prescription, by Royal Charter, and by Act of Parliament. With us they are created by authority of the Legislature, *and not otherwise*. That to establish a corporation is to enact a law; and that no power but the legislative body can do this.

2. That legislative power is vested under our Constitution, in the General Assembly, to consist of a Senate and House of Representatives, to be elected at stated periods by the citizens of the respective counties.

3. And that the General Assembly is bound to exercise the power of making laws thus conferred upon them by the people in the primordial compact, in the mode therein prescribed, and in none other; and that a law made in any other mode is unconstitutional and void. That the Legislature is but the agent of their constituents; and that they cannot transfer authority delegated to them to any other body, corporate or otherwise,—not even to the Judiciary, a co-ordinate department of the government, unless expressly empowered by the Constitution to do so. That to do this would be to violate one of the fundamental maxims of jurisprudence as well as of political science, namely, *delegata potestas non potest delegari*. * * *

4. It was formerly asserted that in England the act of incorporation must be the *immediate* act of the king himself, and that he could not grant a license to another to create a corporation. 10 Reports, 27. But Messrs. Angell and Ames, in their Treatise on Corporations, state that the law has since been settled to the contrary; and that the king may not only grant a license to a subject to erect a particular corporation, but give a general power by charter to erect corporations indefinitely, on the principle that *qui facit per alium facit per se*; that the persons to whom the power is delegated of establishing corpora-

tions, are only an instrument in the hands of the government. 1 Kyd, 50; 1 Black. Com.; Ang. & Am. 63.

Before the revolution, charters of incorporation were granted by the proprietaries of Pennsylvania under a derivative authority from the Crown; and those charters have since been recognized as valid. 3 Wilson's Lectures, 409. A similar power has been delegated by the Legislature of Pennsylvania with regard to churches. 7 S. & R. 517.

The acts of the instrument in these cases become the acts of the mover, under the familiar maxim above mentioned. See also 1 Missouri R. 5.

5. Our opinion is that no legislative power is delegated to the courts by the acts under consideration. There is simply a ministerial act to be performed,—no discretion is given to the courts. The duty of passing the rule or order directing the petition of the corporators to be entered of record on the minutes of the court, setting forth to the public the object of the association and the privilege they desire to exercise, together with the name and style by which they are to be called and known, is made *obligatory* upon the courts; and should they refuse to discharge it, a *mandamus* would lie to *coerce* them. It is true the Legislature has seen fit to use the courts for the purpose of giving legal form to these companies. But it might have been done in any other way. Under the Free Banking Law of 1838, instead of petitioning the court, and having the order passed and entered upon its minutes, the certificate specifying the name of the association, its place of doing business, the amount of its capital stock, the names and residence of the shareholders, and the time for which the company was organized, is required merely to be proven and acknowledged, and recorded in the office of the clerk of the Superior Court, where any office of the association is established, and a copy filed with the Comptroller General. Cobb's Digest, 107, 108.

And so under the Act of 1847, authorizing the citizens of this State, and such others as they may associate with them, to prosecute the business of manufacturing with corporate powers and privileges. The persons who propose to embark in that branch of business are required to draw up a declaration specifying the objects of their association and the particular branch of business they intend carrying on, together with the name by which they will be known as a corporation, and the amount of capital to be employed by them; which declaration is required to be first recorded in the clerk's office of the Superior Court of the county where such corporation is located, and published once a week for two months in the two nearest Gazettes; which being done, it is declared that said association shall become a body corporate and politic, and known as such, without being specially pleaded, in all courts of law and equity in this State, to be governed by the provisions and be subject to the liabilities therein specified. Cobb's Digest, 439, 440.

In these two instances, and others which might be cited, the Legislature have dispensed with the action of the courts, or of any other

agency, to carry out their enactments with regard to these various associations which have become the usual and favorite mode of conducting the industrial pursuits of the civilized world in modern times.

All these Statutes were complete as laws when they came from the hands of the Legislature, and did not depend for their force and efficacy upon the action or will of any other power. It is true that they could only take effect upon the happening of some event, such as the filing the petition or declaration, and giving publicity to the purpose of the association in the mode prescribed by the act. But if this were a good reason for regarding these statutes as invalid, then how few corporations could abide the test! For it requires the *acceptance* of the charter to create a corporate body; for the government cannot compel persons to become an incorporated body without their consent. And this consent, either express or implied, is generally subsequent in point of time to the creation of the charter. And yet, no charter that we are aware of has been adjudged invalid, because the law creating it and previously defining its powers, rights, capacities, and liabilities, did not take effect until the acceptance of the corporate body, or at least a majority of them, was signified.

The result therefore of our deliberation upon this case is, that the Acts of 1843 and 1845, vesting in all associations, except for banking and insurance, the power of self-incorporation, do not impugn the Constitution, and that the charter of the Franklin Bridge Company and all others created under them, and in conformity to their provisions, are legal and valid. With the policy of these Statutes we have nothing to do. The province of this and all other courts is *jus dicere*, not *jus dare*.

*Judgment reversed.**

ATTORNEY-GENERAL v. McARTHUR.

1878. 38 Mich. 204.⁴

Information in the nature of a quo warranto. Argument on general demurrer. Demurrer sustained.

³ Granby Min. Co. v. Richards (1887) 95 Mo. 106; Falconer v. Campbell (1840) 2 McLean (U. S.) 195, *Accord*.

Horton, C. J., in State v. Western Irrigating Canal Co. (1888) 40 Kansas 96, 19 Pac. 349: "The word 'franchise' is generally used to designate a right, or privilege, conferred by law. What is called 'the franchise of forming a corporation', is really but an exemption from the general rule of the common law prohibiting the formation of corporations. All persons in this state have now the right of forming corporate associations upon complying with the simple formalities prescribed by the statute. The right of forming a corporation, and of acting in a corporate capacity under the general incorporation laws, can be called a franchise only in the sense in which the right of forming a limited partnership, or of executing a conveyance of land by deed, is a franchise. (2 Morawetz, Priv. Corp., § 923.)"

Sheldon, J., in Stowe v. Flagg (1874) 72 Ill. 397: "A corporation cannot be constituted by the agreement of parties. It can only be created by or under legislative enactment."—Eds.

⁴ Arguments and portion of opinion omitted.—Eds.

GRAVES, J.—This is an information in the nature of *quo warranto* against the defendants alleging their assumption to act as a corporation by the name and title of "The Cheboygan Slack Water Navigation Company," and that in so doing they usurp the franchise of being a corporation.

The defendants plead actual incorporation on the nineteenth of April, 1867, under the act entitled "An act to provide for the incorporation of slack water navigation companies, for the improvement of rivers in the counties of St. Joseph, Cass, Berrien and Cheboygan and defining their powers and duties." Approved March 25, 1867 (2 Sess. L. 1867, p. 832). To this plea there is a general demurrer in which defendants have joined. Several important questions are mooted in relator's brief which do not arise in this proceeding, and these will not be considered. In disposing of the case we shall adhere strictly to the precise issue raised, and also to the ground, so far as it appears pertinent, which is taken to support the affirmative of it.

What is that issue? It is this, and this only: Are the defendants legally incorporated? No other subject of inquiry is admissible in this proceeding.

The information is filed under Comp. L., 7074, and not under 7085, and it contemplates the case of an assumption by the defendants of the franchise of incorporation without legal right, and consequently that no corporate entity exists to be proceeded against. The complaint is that these persons assume to be incorporated without being so, and therefore the information is against them personally, and not against the artificial being they are charged as unlawfully simulating. Where the information is aimed at alleged corporate delinquencies it supposes and virtually admits corporate existence instead of denying or ignoring it, and the corporation is itself made a party. 7085 *supra*. The law adapts the proceeding to the nature of the case and operates consistently. Under the admission made by the demurrer the defendants must be deemed to be lawfully incorporated unless there are insuperable difficulties in the way and which belong to this act of 1867, and no such difficulties are perceived.

The energies of corporations authorized by it are to be applied and exerted on navigable rivers in a part only of the territory of the State, and as the right is not extended to the whole territory of the State, it is contended by the relator that the enactment infringes part of section one of article fifteen of the constitution, and is therefore wholly void. The provision referred to is as follows:

"Corporations may be formed under general laws; but shall not be created by special act except for municipal purposes."

We think it would be a strained and unreasonable construction to read this clause as requiring all laws for creating corporations not municipal to be so framed as to expressly authorize the corporations in all cases to conduct the specific operations for which they are promoted and established anywhere in the territory of the State. The

language does not fairly imply any such meaning, and we do not understand the clause was designed to compel the Legislature to enact privileges which in the nature of things could not be enjoyed. The great purpose of the provision was to introduce a system of legislation in regard to the institution of corporations which would exclude the corruption and party favoritism which had too often accompanied the method previously in vogue, and to secure as far as practicable for all the people of the State an equality of opportunity and a guard against sectional discriminations. It was determined that corporations of the class in question should owe their erection to general laws and not to special acts, and within this principle, that no law general in form should be allowed to localize the specific work or business of the corporation within narrower bounds than it would naturally be compelled to occupy if not thus localized by enactment. At the same time it was not designed to hinder the confinement of the specific work or business of the corporation by the terms of the law within a given section in any case, when in consequence of natural conditions such work or business could not be carried on elsewhere.

When the provision in question was adopted the system of direct and immediate incorporation of particular individuals by legislative charter, or in other words, the creation of corporations by special act, was generally condemned as impolitic, and those holding this opinion contended that corporations should be organized under common regulations which would permit any group of persons wishing to do so to effect incorporation without special application or special favor, and would exclude sectional distinctions and local immunities and local jealousies, and in this state of opinion the convention framed and the people adopted this section, and if we read it in a sense subservient to the sentiment which then prevailed, we shall give it the construction already suggested, and which its terms as it seems to us fairly bear.

We think the territorial restriction in the act of 1867 is not repugnant to the constitutional provision referred to. The things to be done by corporations which it allows to be created could not be done anywhere else.

* * * * *

We think the defendants are entitled to judgment with costs upon the demurrer.

The other Justices concurred.⁵

⁵ Most of the states by their constitutions forbid the creation of private corporations by special act. The constitutional provisions and the general incorporation laws of the various states will be found digested in Frost's Incorporation and Organization of Corporations, Parker's Corporation Manual, or Stimson's Amer. Stat. Law. As to what objects are authorized by general incorporation laws and how definite the statement of these objects must be, see Machen's Modern Law of Corporations, §§ 48-50.

Maddox, J., in *Lord v. Equitable Life Assur. Society* (1906) 47 Misc. (N. Y.) 187, 94 N. Y. S. 65, at page 70: "Corporations can be created only by some

IN RE WENDOVER ATHLETIC ASSOCIATION.

1911. 70 Misc. (N. Y.) 273, 128 N. Y. S. 561.

IN the matter of the application of the Wendover Athletic Association for the approval of a certificate of incorporation. Approval refused.

GOFF, J.—“A certificate of incorporation must be executed by natural persons, who must be of full age, and at least two-thirds of them must be citizens of the United States, and one of them a resident of this State.” Embraced in this provision (General Corporation Law, § 4) are three essentials of age, citizenship and residence which are applicable to membership corporations. It is provided by § 41 of the membership corporations law that five or more persons may become a membership corporation by making, acknowledging, and filing a certificate stating the name, the object, the location, and the number and names of its directors, and “such certificate shall not be filed without the written approval * * * of a justice of the supreme court.”

It is plain that without such approval the incorporation is absolutely ineffective. What, then, should merit approval? Is the presentation of a certificate containing the bare formula prescribed by the statute sufficient, or should there be proof of compliance with the elemental substance of the law? Strictly speaking, the act of approval by the justice is not a judicial act. It was within the power of the Legislature to confer that authority on any ministerial officer; but having conferred it on a judicial officer it is a legitimate inference that it was so conferred with a purpose, and that is, that the judicial officer from his professional training and habit of thought should apply those tests and rules to the certificate which are applied in judicial procedure in order to ascertain facts, as distinguished

sovereign authority; this may be by a special act or they may be formed under and pursuant to general laws, when authority to so enact shall have been given to the Legislature by appropriate Constitutional provision. When created by special act that act of incorporation is the charter of the corporation so created, while when formed pursuant to the provisions of a general law its charter is the declaration, the certificate or the articles of incorporation, as the case may be, duly executed and filed, after compliance with all the requirements of the statutes in such cases provided. The charter * * * is a continuing grant of corporate power. *Long Island W. S. Co. v. Brooklyn*, 166 U. S. 685, 694. And all applicable provisions of a general law under which a corporation has been formed, not expressly set forth in its certificate or articles of incorporation, are to be read into and taken to be a part of its charter * * *.”

Graves, J., in *Van Etten v. Eaton* (1869) 19 Mich. 187, at page 194: “The organic act under which the corporation was formed, together with the articles of association, are to be considered as the charter of the company, and they are in the nature of a grant from the State to the corporation expressing the rights and privileges conferred and the conditions annexed to them, and the deliberate acceptance of this grant, with the rights and privileges involved in it, is conclusive evidence * * * of knowledge in the grantees or corporators of all those conditions.”—Eds.

from mere assertion, and this inference is strengthened by the nature of the circumstances.

The Legislature has prescribed simple means by which an artificial entity may be created, and, when created, endowed with certain powers and privileges. What more reasonable than that before imparting legal life there should be judicial scrutiny of those qualifications which the law makes essential, and not a mere perfunctory passing on what may be presented. The very act of approval imports that the justice sanctions and accepts as satisfactory the instrument which is required by law to receive his approbation (Black L. Dict.) and this sanction and acceptance cannot be given even to a ministerial act unless there be applied to its performance judicial tests and principles.

Adopting this rule the certificate presented, which is typical of many, recites the desire of the incorporators to form a corporation, they being of full age and at least two-thirds being citizens and one a resident of the State. These are not even conclusions of fact; they are bare assumptions without proof to support them. An illustration of their inutility is furnished by the statement regarding citizenship. It is required that there be five incorporators. How can it be determined which of them constitute the two-thirds that are citizens and which the one-third that is alien? If the term two-thirds of five men be taken literally it will lead to an absurdity. In case of false or erroneous statement it would be impossible to fix responsibility upon the individuals. Their attached acknowledgement would not aid, for that merely certifies to the execution of the paper. This equally applies to the assumption of the residence of one of the signers within the State; which one? Where a number of individuals combine for the purpose of acquiring a corporate existence each one should assume responsibility by submitting proof of the existence of the facts required by law. This should be done by affidavit containing averments, first, by all as to each being of full age; second, by each of them who is a citizen, and third, by the one who is a resident. There should also be an averment as to whether any previous application for incorporation has been made.

It may be pointed out that it is improper to fix a definite date for the holding of the annual meeting, as that date may fall on Sunday, and the law discountenances the use of that day for such purposes.

Approval refused, with leave, however, to renew application upon certificate supported by averments as indicated.

WELLS CO. v. GASTONIA COTTON MFG. CO.

1904. 198 U. S. 177, 49 L. ed. 1003, 25 Sup. Ct. 640.*

THE plaintiff, the W. L. Wells Company, seeks in this action to recover a balance alleged to be due from the defendant, the Gastonia Cotton Manufacturing Company, on account of certain sales of cotton in the years 1899 and 1900.

The complaint averred that the plaintiff and defendant were, respectively, created and duly organized as *corporations*—the former, under the laws of Mississippi; the latter, under the laws of North Carolina.

The defendant admitted that it was a corporation, duly organized under the laws of North Carolina and a citizen and resident of that state, but averred that it had “no knowledge or information sufficient to form a belief as to the truth of the allegation contained in the first section of the complaint, to wit, that the plaintiff is a corporation organized under the laws of the state of Mississippi and a citizen and resident of that state, and, therefore, it denies the said allegation.” The other paragraphs of the answer put in issue the allegation of the complaint touching the plaintiff’s claim against the defendant.

MR. JUSTICE HARLAN, after making the foregoing statement, delivered the opinion of the court.

As the plaintiff was not entitled to maintain its action in the Circuit Court unless it was a corporation of Mississippi, *Great Southern Fire-Proof Hotel Co. v. Jones*, 177 U. S. 449, 454, 456, and the authorities there cited, the denial in the answer of knowledge or information sufficient to form a belief on that point put in issue the plaintiff’s corporate character, within the meaning of the rule, no longer to be questioned, that for purposes of suing and of being sued in the courts of the United States the members of a corporation are to be deemed citizens of the State by whose laws it was created; and as the jurisdiction of the courts of the United States must always appear affirmatively, of record, it became necessary, under existing statutes and under rules of practice and pleading in North Carolina, for the plaintiff to prove that it was a corporation of Mississippi. *Roberts v. Lewis*, 144 U. S. 653, 656; 17 Stat. 196, 197, c. 255, act of June 1, 1872; Rev. Stat. § 914; 18 Stat. 470, c. 137; act of March, 1875; Code of Civil Procedure, N. Car. §§ 133, 243, 260, 276; *Southern Pacific Co. v. Denton*, 146 U. S. 202. It was so held, and correctly, by the Circuit Court of Appeals. 128 Fed. 369.

Was the plaintiff a corporation of Mississippi within the meaning of the above rule? In that state individuals may become incorporated for certain purposes under general laws. The first step there towards incorporation is to apply to the Governor for a charter, stating the purposes for which the corporation is to be created. That

* Statement abridged.—Eds.

officer then takes the advice of the Attorney General as to the constitutionality and legality of the provisions of the proposed charter. If the Governor approves the charter, and causes the Great Seal of the State to be affixed thereto by the Secretary of State, it would seem that the process of incorporation then becomes complete. Charters of incorporation in that State are required to be recorded in the office of the Secretary of State and in the office of the clerk of the Chancery Court of the county in which the corporation does business. Anno. Code of Miss. 1892, c. 25.

It appeared in evidence that W. L. Wells, John T. Wells and George Butterworth submitted to the Governor of Mississippi, to be referred to the Attorney General of the State, the following form of charter:

"§ 1. Be it known and remembered that W. L. Wells, John T. Wells and George Butterworth, their associates and assigns, are hereby created a body politic and corporate, under the name and style of W. L. Wells Company, and by that name shall have succession for fifty years, shall have power to sue and be sued, contract and be contracted with, may have a corporate seal, and break and alter the same at pleasure. § 2. The capital stock of said corporation shall be fifty thousand dollars, divided into shares of five hundred dollars each, and as soon as ten thousand dollars of said stock is subscribed and paid for, said corporation shall have power to commence business. § 3. Said corporation is formed for the purpose of conducting a general cotton business, and may buy and sell cotton, and may transact a cotton factorage business, may advance money or supplies for the purpose of controlling shipments of cotton, may take and receive mortgages or deeds of trust upon property to secure said advances, and generally may have all powers conferred by Chapter 25 of the Annotated Code of 1892 necessary and requisite to carry out the purpose of said corporation. § 4. The board of directors of said corporation shall consist of three persons, whose numbers may be increased at any time by a majority vote of the stockholders, and said directors shall have power to elect all necessary officers, and prescribe the duties, salaries and tenure of such officers."

The Attorney General having certified that the proposed charter of incorporation was not repugnant to the constitution or laws of the State, it was approved by the Governor, and such approval was attested by the Secretary of State, the Great Seal of the State being thereto affixed. The Secretary thereupon certified under the Great Seal that the charter "incorporating the W. L. Wells Company, was, pursuant to the provisions of Chapter 25 of the Annotated Code, 1892, recorded in the Book of Incorporations in this office." It was also recorded in the office of the clerk of the proper Chancery Court.

The contention of the defendants in the court below was—and their contention here is—that the subscription of \$10,000 to the capital stock of the W. L. Wells Company and the payment thereof,

was a condition precedent to the company's becoming a corporation ; that is, it could not become a corporation de jure until such subscription and payment. And this view was sustained by the Circuit Court of Appeals, which said in its opinion: "It is very clear from this that, having a charter like this, conditioned upon the payment of \$10,000 in subscriptions, then these men undertook to exercise powers in the charter without fulfilling or attempting to fulfill the conditions precedent in the charter ; that, even when they had made money in the business, they ignored the corporation altogether, and drew the money out of the business as if it belonged to them, and not to the corporation. The charter never went into operation, and the corporation never became a legal entity. More than this, these assumed corporators went on in business, and contracted obligations in the name of the so-called corporation, which did not possess a dollar of property, or have any mode of meeting a debt, thus seeking to cloak their transactions under an assumed corporate name, and avoid in this way all personal responsibility. At the same time two of them were, in a business sense, irresponsible. It would seem that this transaction was an abuse of, and in fraud of, the law. And that the Wells Company had never, and could not have, any legal existence. When a corporation is formed under an enabling act, all the mandatory provisions of the statute must be complied with." 128 Fed. 369, 372.

We are of opinion that the Circuit Court of Appeals erred in holding that the charter of the W. L. Wells Company made it a condition of its becoming a corporation that \$10,000 of capital stock should be subscribed and paid for. The question was not as to the good faith of the incorporators, nor whether the company was organized in fraud of the law. Those were not matters to be inquired into in ordinary suits between the company and individuals or incorporations. If the organization of the company as a corporation was tainted with fraud, it was for the State, by some appropriate proceeding, to annul its charter. The question before the court below was whether the company was, technically, a corporation, and that depended upon the legal effect of the words of its charter. The first section of that charter expressly declares that the incorporators, their associates and assigns, "are hereby created a body politic and corporate, under the name and style of W. L. Wells Company, and by that name shall have succession for fifty years, shall have power to sue and be sued, contract and be contracted with, may have a corporate seal, and break and alter the same at pleasure." These words can have but one meaning. They manifest the purpose of the legislature to create a corporation. Substantially the same words in a charter granted by Congress were held to create a corporation. *Minor v. Mechanics' Bank of Alexandria*, 1 Pet. (U. S.) 46, 63. The second section of the company's charter did not modify the provisions of the first section. It did not require the payment of a given amount of stock subscriptions be-

fore the company should be considered in esse as a corporation. It did nothing more than confer the privilege or power of commencing business when a specified amount, less than the whole, of its authorized capital stock was subscribed and paid for. The company was created a corporation by the previous section, with power in its corporate name to sue and be sued, contract and be contracted with; and, under the general statutes of the State, it came into existence as a corporation immediately upon its charter being approved by the Governor of Mississippi and such approval certified by the Secretary of State under the Great Seal of the State. If the commencing of the business for which it was incorporated before a certain amount of capital stock was subscribed and paid for was in violation of the company's charter, that was a matter for which it could be called to account by the State, and did not affect the existence in law of the company as a corporation. Of course, if the charter of the company had made it a condition precedent to its becoming a corporation that a certain amount of capital stock should be subscribed and paid for, a compliance with that condition would have been necessary before the company would have become a corporation entitled to sue and be sued in the courts of the United States. But, as we have seen, the charter in question prescribed no such condition. If the legislature had intended to withhold corporate existence until a given amount of capital stock was subscribed and paid for, that intention, we may assume, would have been manifested by clear language. We do not feel at liberty, by mere construction, to qualify the explicit declaration in the first section of plaintiff's charter as to the corporate existence thereby created. We therefore hold that under the statutes of Mississippi the only conditions precedent to the existence of the corporation were the approval by the Governor of the State of its proposed charter and the certification of that approval under the Great Seal of the State.

It is said that the interpretation we have given to the charter of the W. L. Wells Company is not in harmony with the principles announced by the Supreme Court of Mississippi. We are referred in support of this view to *Perkins v. Sanders*, 56 Mississippi, 733, 738, 739, which was a suit by a creditor to enforce the personal liability of stockholders for the debts of a certain company. But there is nothing in that case clearly indicating that the Supreme Court of Mississippi would, if this question were before it, hold the requirement of the subscription of \$10,000 of stock and its payment before commencing business to have been a condition precedent to the plaintiff becoming a corporation. That court, in the case cited, referred to a section of the charter of the company there in question, providing that the persons named in it, and all others who then were or might thereafter become associated with them, and their successors and assigns, "be, and they are hereby, created a body politic and corporate, under the name," etc.,—a provision like that found in the plaintiff's charter. The court said: "This was no proposition

to create a corporation upon the performance of certain conditions, but it was itself the creation of a corporation, requiring no other act to be performed by the corporators than their acceptance of the charter, and this even was unnecessary, if, as it is probable, the corporators had applied for the grant of the charter and thus accepted it in advance. * * * The distinction between the two classes of charters is thus seen to be that in the first class the charter is mere permission on the part of the legislature for the formation of a corporation upon the doing of certain acts prescribed in the charter as precedent conditions, and, as a necessary result, no corporate act can be done until those conditions have been performed, except such as may be expressly permitted by the charter; and, as to those acts, it would be considered that the corporation had an existence before its full investiture with its corporate franchises. In the latter class in which is this company the corporation is in existence for all the purposes of its creation from the beginning, except so far as there may be restraints placed on it by the charter, either expressly or by plain implication."

It thus appears that the Supreme Court of Mississippi, in the case referred to, decided that where acts are required to be performed before the corporation comes into existence, no corporation is created or can exist until those acts are performed. In this general view we entirely concur. But the question remains whether the particular charter here in question made it a condition precedent to the existence of the W. L. Wells Company as a corporation, that a certain amount of its capital stock should be subscribed and paid for. As already indicated, we are of opinion that no such condition precedent was prescribed, and that under the statutes of Mississippi and independently of the subscription of a certain amount of stock and its payment, the plaintiff became, in law a corporation when the Governor approved its charter and the fact of such approval was certified by the Secretary of State under the Great Seal of Mississippi. It could not thereafter dispute its liability for acts done by it in its corporate name nor be denied the right to sue in that name.

As the Circuit Court of Appeals proceeded on different grounds as to the jurisdiction of the Circuit Court, its judgment must be reversed, and the case remanded, with directions to that court to set aside its own judgment, and for such further proceedings touching the merits of the case as may be consistent with this opinion and with law.

*Reversed.*⁷

⁷ Johnson v. Kessler (1888), 76 Ia. 411; Palmer v. Lawrence (1849), 3 Sandf. Super. Ct. (N. Y.) 161, esp. 172-4; Schenectady, etc., Road Co. v. Thatcher (1854), 11 N. Y. 102; National Bank v. Texas Investment Co. (1889), 74 Tex. 421, *Accord.* Cf. Aspen Water and Light Co. v. City of Aspen (1894) 5 Colo. App. 12.

Sometimes the subscription of all, or a certain prescribed amount, of the capital stock, is expressly constituted a condition precedent to *de jure* incorporation; see, for example, Rev. St. Ill., Chap. 32, sec. 4, requiring that all the

BUTLER PAPER CO. v. CLEVELAND

1906. 220 ILL. 128, 77 N. E. 99.

MR. JUSTICE SCOTT delivered the opinion of the court.

This suit was brought in the superior court of Cook county by the J. W. Butler Paper Company against Frederick W. Chamberlain, Harold I. Cleveland and Harriet F. Cleveland, to recover the sum of \$1,305.80 alleged to be due the plaintiff for merchandise sold by it to the defendants as officers and directors of the C. & C. Company, a corporation organized under the statute of this state. Chamberlain was a resident of the state of Michigan, and process was not served upon him. The other two defendants entered their appearance and filed the general issue to the plaintiff's declaration. A trial was had before the court without a jury, by agreement of the parties, upon a stipulation of facts, and the court found the issues in favor of the defendants, and, after overruling a motion for a new trial, entered judgment against the plaintiff for costs of suit. The plaintiff appealed to the Appellate Court for the First District, and that court having affirmed the judgment of the superior court, a further appeal has been prosecuted to this court.

The only question arising upon the record in the case, which is presented by certain propositions of law offered by the plaintiff below and refused by the court, is whether there was such a failure to comply with the provisions of "An act concerning corporations," (approved April 18, 1872, in force July 1, 1872), in organizing the C. & C. Company, of which the defendants were officers and directors at the time the merchandise was sold by the plaintiff to the C. & C. Company, as to render the defendants individually liable to the plaintiff therefor under section 18 of chapter 32, Hurd's Revised Statutes of 1903. That section, which was construed by this court in *Loverin v. McLaughlin*, 161 Ill. 417, reads as follows:

"If any person or persons being, or pretending to be, an officer or agent, or board of directors, of any stock corporation, or pretended stock corporation, shall assume to exercise corporate powers, or use the name of any such corporation, or pretended corporation, without complying with the provisions of this act, before all stock named in the articles of incorporation shall be subscribed in good faith, then they shall be jointly and severally liable for all debts and liabilities made by them, and contracted in the name of such corporation or pretended corporation."

The sole ground relied upon by the plaintiff as showing a defective incorporation of the C. & C. Company is the fact that the meeting of the subscribers to the capital stock of the company, held for the purpose of electing directors and for the transaction of such

capital stock be subscribed and at least one-half thereof paid in, before the Secretary of State may issue a certificate of complete organization.—Eds.

other business as might come before them, was not called in the manner pointed out by the statute.

Section 3 of chapter 32, *supra*, provides that notice of such meeting shall be given "by depositing in the postoffice properly addressed to each subscriber, at least ten days before the time fixed, a written or printed notice, stating the object, time and place of such meeting."

Frederick W. Chamberlain, Harold I. Cleveland and Harriet F. Cleveland were the only subscribers to the capital stock of the C. & C. Company. The license to open books of subscription to the capital stock of the company was issued on December 10, 1902. On December 12, 1902, the three subscribers above named executed a written instrument by which they waived the notice provided for by section 3, *supra*, and requested the commissioners to convene the meeting at 12 o'clock, noon, of that day at Room 913 Monadnock block, in the city of Chicago, for the purpose of electing directors and transaction of such other business as might come before them. Prior to the meeting, in pursuance of this written instrument, a notice was personally delivered to each of the three subscribers, notifying them of the object, time and place of the meeting. The subscribers met at the time and place specified and elected a board of directors, consisting of themselves and George A. Miller, who was one of the commissioners to whom the license had been issued by the Secretary of State.

A decision of this case depends upon the question whether the C. & C. Company is a corporation *de jure*. Proof of a corporation *de facto* does not relieve the directors and officers of the corporation from the liability imposed by section 18, *supra*. There must be a corporation *de jure* in order to escape that liability. *Loverin v. McLaughlin*, 161 Ill. 417; *Gunderson v. Illinois Trust and Savings Bank*, 199 Id. 422.

The statute prescribes a certain course to be pursued in organizing a corporation in this state. It does not necessarily follow, however, that any departure from that course will prevent a corporation from becoming one *de jure*. Whether or not such departure will have that effect depends upon the nature of the provision which is violated. If it is a mandatory provision, a failure to substantially comply with its terms will prevent the corporation from becoming one *de jure*; but if the provision is merely directory, then a departure therefrom will not have that consequence.

In Cooley's Constitutional Limitations (star page 78) it is said: "Those directions which are not of the essence of the thing to be done, but which are given with a view merely to the proper, orderly and prompt conduct of the business, and by a failure to obey which the rights of those interested will not be prejudiced, are not commonly to be regarded as mandatory; and if the act is performed, but not in the time or in the precise mode indicated, it may still be sufficient, if that which is done accomplishes the substantial purpose of the statute."

The provision of the statute here under consideration, requiring notice of the first meeting to be given to the subscribers to the capital stock of a corporation being organized, by mailing to them notices stating the object, time and place of such meeting at least ten days before the time fixed for such meeting, is evidently intended only as a direction "given with a view merely to the proper, orderly and prompt conduct" of the commissioners in calling such meeting, and a failure to obey that provision will not prejudice the rights of any persons interested therein if the same result is reached in some other mode. The only persons interested in the result to be attained by giving notice of the object, time and place of a meeting of the subscribers to the capital stock of a corporation for the purposes specified in the statute are the subscribers themselves. We perceive no reason why such persons, where all agree thereto, may not waive the giving of the statutory notice, if the meeting is actually held, as the purpose of the statute in requiring the notices to be given has in such case been accomplished.

The mere fact that the word "shall" is used in the statute in providing for the notice does not render the provision mandatory. *Canal Commissioners v. Sanitary District*, 184 Ill. 597.

In the case of *Newcomb v. Reed*, 12 Allen, (Mass.) 362, in discussing the effect upon the legality of a corporation where the call for the first meeting was signed by only one of the persons named in the act of incorporation instead of by a majority of such persons, as required by the statute of Massachusetts, the court said: "The organization was not strictly regular, but can hardly be considered even as defective. And if the object of the statute is regarded, by which it is required that the first meeting shall be called by a majority of the persons named in the act of incorporation, it will be evident that it is directory, merely, and only designed to secure the rights conferred by the charter to those to whom it was granted, among themselves, by providing an orderly method of organization. Thus, if all the persons interested should come together without any notice or call whatever, and proceed to accept the charter and do the other acts necessary to constitute the corporation, we cannot doubt that their action would be valid, and that neither the public, nor any persons not belonging to the association, would have any interest to question their proceedings. The purpose of the statute was probably to avoid such difficulties as were disclosed in the case of *Lechmere Bank v. Boynton*, 11 Cush. 369, where two parties had attempted to organize separately under the same charter, each claiming to be the corporation."

Cases have also arisen in this state in which the effect of a failure to give notice of corporate meetings in the manner provided by statute have been considered and it has been uniformly held that it is immaterial whether or not such notice has been given in the manner pointed out by the statute, if the persons entitled to such notice actually attend the meeting and participate in the business there

transacted. *Thomas v. Citizens' Horse Railway Co.* 104 Ill. 462; *Gade v. Forest Glen Brick Co.* 165 Id. 367.

This case is distinguishable from *Loverin v. McLaughlin*, supra, which is relied upon by appellant, in that notice of the first meeting of subscribers is not intended for the benefit of the public, as no publicity of such meeting is required, but is merely for the benefit of the subscribers, while in the *Loverin* case the provision which was not complied with was that requiring the certificate of complete organization issued by the Secretary of State to be filed and recorded in the office of the recorder of deeds of the county in which the principal office of the corporation is located, and a compliance with the statute in that regard was essential because the provision was one for the benefit of the public, and could not be waived.

It is urged that the fact that section 4 of the act in question requires a copy of the notice provided for by section 3, supra, to be included in the report made to the Secretary of State, shows that the statute contemplates compliance with the statute in regard to giving notice. We think this provision is fully satisfied by including in such report the written instrument signed by all the subscribers in which such notice is waived.

The superior court did not err in refusing the propositions of law and in entering judgment upon the stipulation of facts in favor of the defendants and against the plaintiff for costs.

The judgment of the Appellate Court will be affirmed.

*Judgment affirmed.*⁸

Section 2.—Corporations of Two or More States.

QUINCY RAILROAD BRIDGE CO. v. COUNTY OF ADAMS.

1878. 88 Ill. 615.

MR. JUSTICE BREESE delivered the opinion of the court:

This was an action of debt, brought to the Adams Circuit Court, by the county of Adams, plaintiff, and against the Quincy Railroad Bridge Company, defendants, to recover a tax assessed against the capital stock of the bridge company for the year 1874, for county purposes. There were two special counts and the common counts

⁸ *Mokelumne &c. Mining Co. v. Woodbury* (1859) 14 Cal. 424; *Humphreys v. Mooney* (1880) 5 Colo. 282; *Newcomb v. Reed* (1866) 12 Allen (Mass.) 362; *Walworth v. Brackett* (1867) 98 Mass. 98; *Braintree Water Co. v. Braintree* (1888) 146 Mass. 482, 16 N. E. 420, *Accord*.

The general incorporation laws required the insertion in the articles of the number and names of the directors. These were omitted. *Held*, the provision was imperative and not merely directory and that the plaintiff company could not recover upon a subscription to its capital stock. *Reed v. Richmond St. Ry. Co.* (1875) 50 Ind. 342. So, also, where the corporate name was omitted. *Piper v. Rhodes* (1868) 30 Ind. 309; *Rhodes v. Piper* (1872) 40 Ind. 369.

in the declaration, to which the defendants pleaded seven pleas: 1. *Nil debet*. 2. *Nul tiel corporation* as to the bridge company. 3. That it is a corporation created and existing under the laws of this state and of the state of Missouri, and not otherwise. 4. That defendant is a corporation created for the purpose of constructing and maintaining a railroad bridge over and across the Mississippi river, under the laws of Illinois and Missouri, the said river forming a boundary between these states, and that the corporate powers and existence of the defendant company are under and by virtue of the laws of this state only in part. 5. That no proper demand was ever made for the supposed taxes prior to the commencement of this suit. 7. That the collection of this tax was heretofore enjoined by an order of the Circuit Court of the United States for the Northern District of Illinois in a suit therein, in which one Nathaniel Thayer was plaintiff, and Edwin Cleveland, then the collector of Adams county, and this bridge company, were defendants, which order is still in force. The court sustained a general demurrer to these special pleas. Leave was given to amend the seventh plea, which was done by setting out more fully the injunction allowed by the circuit court of the United States, and to this amended plea a general demurrer was sustained by the court. The cause then proceeded to trial, which resulted in a judgment in favor of the county for the amount of taxes claimed. To reverse this judgment the bridge company appeal, and make the point that appellants are not a company or association incorporated under the laws of this state in the sense or spirit of the law authorizing the taxation of capital stock.

The demurrer to the special pleas clearly presents this question, and it has been argued elaborately and ably by counsel: Are appellants a corporation so created under the laws of this state as to bring it under the operation of the fourth clause of section one of the Revenue act of 1872?

The first section provides that the property named in this section shall be assessed and taxed, except so much as in this act may be exempted: *First*, all real and personal property in this state. *Second*, all money, credits, bonds or stocks, etc. *Third*, the shares of capital stock of banks and banking companies doing business in this state. *Fourth*, the capital stock of companies and associations incorporated under the laws of this state. Rev. Stat. 1874, p. 857.

Appellants give the history of the creation of their company, by which it will be seen that by an act of the General Assembly of this state, approved February 10, 1853, and renewed by act of Feb-

In *People v. Montecito Water Co.* (1893) 97 Cal. 276, where the acknowledgment of their signatures to the articles by the incorporators was held a condition precedent to *de jure* incorporation, the court said: "As this is an express condition precedent to a valid incorporation, it is not of consequence to the court whether it be a wise or necessary requirement or not." See also *People v. Selfridge* (1877) 52 Cal. 331.—Eds.

ruary 15, 1865, the Railroad Bridge Company was incorporated. By an act of the legislature of the state of Missouri, date not given, the "Quincy Bridge Company" was incorporated, the object and purpose of both these incorporations being to construct and operate a railroad bridge across the Mississippi river at Quincy, in this state, such object not being attainable by either company separately or by virtue of the authority thus granted by either state, the river being a common boundary, and the territorial line of neither state extending beyond the main channel of the river. Appellants say, in order to render either of these charters available, it became necessary to consolidate the two companies, and to secure for the company thus consolidated the consent and approval of each of said states, and the permission of the government of the United States to throw a bridge across one of its navigable rivers.

On November 20, 1866, articles of agreement were entered into by these two companies thus incorporated, one by this state, the other by the state of Missouri, to consolidate, and such articles, duly filed and recorded in the office of the Secretary of State of this state, effected the consolidation of these two companies, and such consolidation was approved and legalized by the General Assembly of this state by an act, approved February 6, 1867, entitled "An act to legalize the Quincy Railroad Bridge Company, and to facilitate and encourage the construction of a railroad bridge over the Mississippi river at Quincy." The first section of this act recognizes the consolidation of these two independent companies and their origin, and refers to the articles of consolidation on file in the office of the Secretary of State of this state, and the name and style of the Quincy Railroad Bridge Company was bestowed upon it, and there was conferred upon it all the rights, powers, privileges and immunities which were granted to the railroad bridge company by the act incorporating the same in 1853, and renewed in 1865.

The consolidation of these companies is expressly recognized, and by the second section the company, as now existing, is fully recognized after the consolidation as a corporation. What is wanting to make appellants a corporation created by the laws of this state, we are unable to see.

But it is said by appellants, this corporation, although it derived some of its powers and in part its corporate existence from this state, derived an equal part from the sovereign state of Missouri, and therefore they are not a corporation created under the laws of either state. To this it is answered, and we think satisfactorily, that the legislatures of this state and of Missouri cannot act jointly, nor can any legislation of the last named state have the least effect in creating a corporation in this state. Hence, the corporate existence of appellants, considered as a corporation of this state, must spring from the legislation of this state, which, by its own vigor, performs the act. The states of Illinois and Missouri have no power to unite in passing any legislative act. It is impossible, in the very

nature of their organizations, that they can do so. They cannot so fuse themselves into a single sovereignty, and as such create a body politic which shall be a corporation of the two states, without being a corporation of each state or of either state. As argued by appellee, the only possible *status* of a company acting under charters from two states is, that it is an association incorporated in and by each of the states, and when acting as a corporation in either of the states it acts under the authority of the charter of the state in which it is then acting, and that only, the legislation of the other state having no operation beyond its territorial limits. We do not, and cannot, understand that appellants derive any of their corporate powers from the legislature of the state of Missouri, but wholly and entirely derived from the General Assembly of this state. Consequently they are embraced in the first section of the revenue act, above cited.

It is argued by appellants, that the framers of the Revenue act of 1872 did not intend to include them in the general designation of "companies or organizations incorporated under the laws of this state," and this is apparent from the fact, that within a year after that law went into effect the legislature provided, in explicit terms, for the taxation of the property of the class of corporations to which their company belongs.

The reference is to the act of May 1, 1873, entitled "An act to provide for the assessment and taxation of bridges across navigable waters on the borders of this state."

We do not perceive this act has any relation to the question raised on this record. The act applies solely to bridge structures, and capital stock is not mentioned in it. The sole object, as appears from its various clauses, especially the emergency clause, was to declare such structures real estate, they, before that time, having been regarded as personal property. This is seen by § 15 of the "act for the assessment of property and for the levy and collection of taxes," in force July 1, 1872. That section provides that the track, road or bridge shall be held to be personal property, and listed and assessed as such in the town, district, village or city where the same is located or laid. Sess. Laws, 1872, p. 5.

The emergency clause in the act of 1873 conclusively determines the purposes for which the act was passed. That clause is as follows: "Whereas, by existing law, such bridge structure can not be sold for delinquent taxes, so as to convey a good title thereto, therefore an emergency," etc. Nothing appears in any of the provisions of this act expressly or impliedly exempting the companies owning such structures from the payment of taxes upon their capital stock.

It is further argued by appellants that the legislature intended to limit the tax of capital stock to companies exercising corporate powers wholly and solely under the laws of this state. Appellants say this is evident from the fact that the capital stock of companies ex-

isting in part by virtue of the laws of a sister state, cannot be equitably assessed or collected.

We fail to perceive this supposed dilemma. Precise and exact equity cannot, perhaps, be done to any corporation in the assessment of its capital stock, but there can be no more difficulty in doing so with such a corporation as appellants, than with any other corporation, and although the capital stock of appellants may designate its entire property, as well in Missouri as in this state, the same may be said of all other corporations having property in different states. This is no reason why the capital stock should not be taxed at all. Suppose, as suggested by appellants, the capital stock of appellants should be assessed and taxed by the authorities of the state of Missouri, would it follow the law of our state is therefore invalid and must not be enforced? Capital stock, or that kind of property designated as such, is not the identical lands, chattels and other articles of property possessed by the corporation, but as this court defined it, in *Porter et al. v. Rockford, &c., R. R. Co.*, 76 Ill. 561, means, as used in the act of 1872, not shares of stock, either separately or in the aggregate, but one intended to designate the property of the corporation subject to taxation, not in separate parcels, but as an homogeneous unit, partaking of the nature of personality, and subject to the burdens imposed upon it at the domicile of the owner.

Who, in this case, is the appellant corporation, and whose domicile is here, where it exercises corporate franchises, where its business is done, where its franchises are exercised, and where it is engaged in the prosecution of the corporate enterprise? *Bristol v. Chicago, &c., R. R. Co.*, 15 Ill. 436. However this corporation may be treated by the authorities of the state of Missouri, the authorities of this state must regard and treat the company as domiciled here, and liable to taxation upon all its property which is of such a nature as to be taxable at the residence of the owner. There is no evidence in the record that appellants have been overassessed or taxed, or that the slightest injustice has been done to appellants.

There is no need to pursue this discussion further. We hold appellant is a corporation created under the laws of this state, and its capital stock properly taxable, and properly assessed and taxed, and the judgment of the circuit court was right and must be affirmed.

*Judgment affirmed.*¹

¹ In *People v. New York &c. R. Co.* (1892) 129 N. Y. 474, 29 N. E. 959, held that the defendant corporation, being a consolidation under a New York statute of railway companies organized under the laws of New York, Pennsylvania, Ohio and Indiana, was not subject to a tax upon its aggregate capital stock under the terms of an act imposing an organization tax on railroads "incorporated under the laws of New York." At page 484, Andrews, J., said: " * * * the new corporation would owe its existence not to the state of New York alone, but to the states of New York, Pennsylvania, Ohio and Indiana. It would not be in any strict or even just sense a corporation 'incorporated by or under any general or special law of this state,' within chapter 143 of the

RAILROAD v. BARNHILL.

1892. 91 TENN. 395, 19 S. W. 21.

CALDWELL, J.—This is a garnishment proceeding, by which J. T. Barnhill seeks to recover from the Mobile and Ohio Railroad Company, as garnishee, the sum of \$50.60, due from it to his debtor, J. J. Joyner.

The circuit judge tried the case on an "agreed statement of facts," and rendered judgment in favor of Barnhill. The railroad company appealed in error.

In its answer, the railroad company admits that it is indebted to Joyner in the sum of \$52.60, but denies that it is subject to garnishment in the state of Tennessee for that indebtedness.

The facts upon which the defense is made are as follows: That the Mobile & Ohio Railroad Company was chartered originally by the state of Alabama, then by the state of Mississippi, and then by the state of Tennessee; that the indebtedness of the company "to Joyner is for labor performed wholly within the state of Mississippi," and under contract made in that state, and that he is a citizen of that state.

Barnhill is a resident of Tennessee; and the garnishment process, which is in due form, was regularly served on the station agent of the railroad company at Ramer, in McNairy county, this state.

From these facts the argument is made that the railroad company, as well as Joyner, is a non-resident of Tennessee and a resident of Mississippi as to the subject-matter of this litigation, and that therefore the courts of this state have no jurisdiction to render judgment against it for the debt in question.

It is true, as a general rule, that a non-resident cannot be charged as garnishee; but it is not true that the railroad company is to be treated, in this case, as a non-resident. In reality it is not a non-resident, but a resident of Tennessee. It exists and performs its functions within our territorial limits as a domestic corporation, by virtue of a charter granted by the legislature of this state. Acts 1847-48, Ch. 118.

That the same incorporators obtained earlier charters from the states of Alabama and Mississippi, and effected an organization and

Laws of 1886. The Consolidation Act does, indeed, confer new corporate powers upon the New York corporation. Except for that act it could not have entered into the agreement of consolidation. So, also, it purports to grant corporate powers to the consolidated company. But it remains true, nevertheless, that concurrent legislation of the other states was essential to the completion of the consolidation, and it is to be inferred from the agreed statement that similar legislation to the act of 1869 was enacted in the several states."

See also *Chicago &c. R. Co. v. Auditor General* (1884) 53 Mich. 79; *Ohio &c. R. Co. v. Wheeler* (1861) 1 Black (U. S.) 286; *Nashua &c. R. Corp. v. Boston &c. R. Corp.* (1890) 136 U. S. 356, 34 L. ed 363, 10 Sup. Ct. 1004.—Eds.

still do business thereunder, does not render the corporation any less a resident of Tennessee.

It is well settled that a corporation created and organized under the laws of a particular state has its legal residence in that state, and that it cannot change its citizenship by doing business in another state. *Baltimore and Ohio R. R. Co. v. Koontz*, 14 Otto, 5.

"It must dwell in the place of its creation, and cannot migrate to another sovereignty." *Bank of Augusta v. Earle*, 13 Peters, 520.

Yet different charters for the same general business may be granted by different states to the same incorporators; and when that is done, and organization is properly effected under each charter in succession, the corporation becomes a citizen of each state, and, as such, has the protection of and is amenable to her laws. *Memphis and Charleston Railroad Company v. State of Alabama*, 107 U. S. 581.

The fact that the indebtedness of the railroad company to Joyner arose in Mississippi, under a contract made in that state, does not render the railroad company a non-resident of Tennessee as to that indebtedness. The contention to the contrary, and that the railroad company is a non-resident of this state as to that debt, is not sustained by the case of *Memphis and Charleston Railroad Company v. State of Alabama*, 107 U. S. 581.

The decision in that case was that the railroad company was a citizen of both Tennessee and Alabama, having been chartered in each state; and that, being a citizen of Alabama, it could not, upon the ground of citizenship in Tennessee, remove into the Circuit Court of the United States a suit brought against it in a state court of Alabama by another citizen of Alabama.

It was *not* there decided, as here contended, that, for the purposes of that litigation, the corporation was to be treated as not a citizen of Tennessee because the matters involved arose in Alabama. The ground of that decision was corporate citizenship in Alabama, the court holding that the corporation was a citizen of that state as well as of Tennessee, where it obtained its first charter.

The *Mobile & Ohio Railroad Company*, as already stated, was chartered and is doing business in Alabama, Mississippi and Tennessee. It is, therefore, in fact and in law a citizen of each of these states.

Whether the debt here involved was created in this state or in the state of Mississippi, is a question which cannot affect the citizenship of the corporation in Tennessee, or the jurisdiction of the courts of this state to render proper judgment against it as garnishee in this case.

Nor does the non-residence of Joyner, the creditor of the railroad company and debtor of plaintiff below, defeat or preclude the jurisdiction of our courts. Clearly, Joyner himself could have come into Tennessee and maintained his suit here against the railroad company for its indebtedness to him. He could have obtained jurisdic-

tion of the corporation by service of process upon its proper officer or agent in this state. Code § 2831 et seq. That being so, it would seem to follow that his creditor can by service upon the same person bring the corporation before the court, and there have the same question of liability adjudged.

Even as against a foreign corporation doing regular business in this state, the present proceeding would be within the rules of procedure laid down in a recent work of high standing. The language of the work referred to is as follows:

"The question of the liability of foreign corporations to garnishment differs little from that of natural persons domiciled in another jurisdiction, in so far as the course of business of certain classes of corporations has occasioned the enactment of special statutes in most of the states, giving courts jurisdiction of such bodies when engaged in the prosecution of their business in states other than that of their residence.

"Except, therefore, in those states where it is held that corporations are in no event subject to garnishment, a foreign corporation may be charged as garnishee in all cases where an original action might be maintained against it for the recovery of the property or credit in respect to which the garnishment is served. In some of the states this rule obtains through the construction of statutes *pari materia*, and in others by express provision. Generally, the jurisdiction of the court in such cases is based upon a statute providing for the commencement of suits against foreign corporations when engaged in doing business within the State, by service upon some officer or agent of the company resident there or that may be found within the jurisdiction." 8 Am. and Eng. Ency. of Law, 1131, 1132.

In this state there is just such a statute as that referred to in the last sentence above. Code §§ 2831 to 2834a inclusive. It comprehends both domestic and foreign corporations. *Railroad Company v. Walker*, 9 Lea, 480; 16 Lea, 418.

In any and every aspect of the case at bar the plaintiff in error is subject to be charged as garnishee.

The same question, upon very similar facts, came before this court in *Holland v. Mobile and Ohio Railroad Company*, 16 Lea, 414. The conclusion reached in that case was the same as that reached in this. A mere citation of that case would have been sufficient for the purposes of this one, but for the fact that counsel has questioned the soundness of the decision there made, and asked to have the question re-examined.

Believing it to be entirely sound, we adhere to the ruling made in that case. In the conclusion of the opinion, the court speaking through Judge Cooper, said: "All of the authorities agree, therefore, that in the case of a railroad corporation chartered by two or more states the corporation may be garnished in each state for

wages due by it to its employes. Drake on Attachments, Sec. 879; 1 Rorer on Railroads, Sec. 720." 16 Lea, 418.

*Affirmed with costs.*²

GOODWIN v. NEW YORK, ETC., R. CO.

1903. 124 FED. 358.

LOWELL, District Judge.—This is an action of tort brought by a citizen of Massachusetts against "the New York, New Haven & Hartford Railroad Company, a corporation duly established by the laws of the state of Connecticut," to recover for injuries sustained in Massachusetts. The officer's return to the writ states that it was served "by delivering in hand to Fayette S. Curtis, fourth vice-president thereof, at his office in said Boston, the original summons of this writ." The defendant has pleaded to the jurisdiction, and the issue raised by the plea has been tried upon agreed facts. The court has to determine if there is diversity of citizenship between the plaintiff and the defendant. The matter has been so much discussed in opinions rendered by the Supreme Court and by other federal courts, and the dicta, if not the decisions, are so contradictory, that a somewhat extended examination of the question must be made.

In the United States a single railroad system often extends into several states. The system is most conveniently operated by one organization, and the courts have had to determine what is the relation of this organization to the several states in which its lines are situated. In *Martin v. B. & O. R. R.*, 151 U. S. 673, 677, 14 Sup. Ct. 533, 38 L. ed. 311, it was said:

"A railroad corporation, created by the laws of one state, may carry on business in another, either by virtue of being created a corporation by the laws of the latter state also, as in *Railroad Co. v. Vance*, 96 U. S. 450 (24 L. ed. 752); *Memphis & Charleston Railroad Co. v. Alabama*, 107 U. S. 581 (2 Sup. Ct. 432, 27 L. ed. 518); *Clark v. Barnard*, 108 U. S. 436 (2 Sup. Ct. 878, 27 L. ed. 780); *Stone v. Farmers' Co.*, 116 U. S. 307; and *Graham v. Boston, Hartford & Erie Railroad*, 118 U. S. 161 (6 Sup. Ct. 1009, 30 L. ed. 106); or by virtue of a license, permission or authority granted by the laws of the latter state to act in that state under its charter from the former state. *Railroad Co. v. Harris*, 12 Wall. 65 (20 L. ed. 20); *Railroad Co. v. Koontz*, 104 U. S. 5 (26 L. ed. 643); *Pennsylvania Railroad v. St. Louis, etc., Railroad*, 118 U. S. 290 (6 Sup. Ct. 1094, 30 L. ed. 83); *Goodlett v. Louisville & Nashville Railroad*, 122 U. S. 391 (7 Sup. Ct. 1254, 30 L. ed. 1230); *Marye*

² See *Wabash Railroad Co. v. Dougan* (1892) 142 Ill. 248, 31 N. E. 594. Cf. *Central Trust Co. v. Chattanooga &c. R. Co.* (1895) 68 Fed. 685.—Eds.

v. Baltimore & Ohio Railroad, 127 U. S. 117 (8 Sup. Ct. 1037, 32 L. ed. 94). In the first alternative it cannot remove into the Circuit Court of the United States a suit brought against it in a court of the latter state by a citizen of that state because it is a citizen of the same state with him. *Memphis & Charleston Railroad v. Alabama*, above cited. In the second alternative it can remove such a suit, because it is a citizen of a different state from the plaintiff. *Railroad Co. v. Koontz*, above cited."

For purposes of convenience, the two classes of corporations above described will be designated in this opinion as the first and the second, respectively. It is not necessary here to consider by what marks the two classes are distinguished, because the Circuit Court for this district in *Smith v. New York, New Haven & Hartford Railroad* (C. C.) 96 Fed. 504, has decided that the railroad here in question is of the first class.

The classification just mentioned has been modified in one particular by later cases. A corporation of the second class, created by the laws of one state, may have become a corporation of another state into which its lines extend; but its incorporation in the latter state, though rendering it subject for many purposes to the laws of that state, is not deemed to affect its jurisdictional status. Thus in *St. Louis & San Fran. Railway Co. v. James*, 161 U. S. 545, 16 Sup. Ct. 621, 40 L. ed. 802, the plaintiff in error was a railroad corporation created in Missouri, and therefore a citizen thereof. It owned and operated lines of railroad in Arkansas, and by virtue of the general statutes of Arkansas had "become a railroad corporation of (Arkansas), subject to all the laws of the state now in force or hereafter enacted, the same as if formally incorporated in this state, anything in its articles of incorporation or charter to the contrary notwithstanding, and such acts on the part of such corporation shall be conclusive evidence of the intent of such corporation to create and become a domestic corporation." Yet it was held not to be a citizen of Arkansas, so as to permit suit in the Circuit Court in that state brought against it by a citizen of Missouri. Incorporation for some purposes in Arkansas was not deemed to affect the defendant's sole jurisdictional citizenship in Missouri. Again, in *Louisville Railway Co. v. Louisville Trust Co.*, 174 U. S. 552, 563, 19 Sup. Ct. 817, 43 L. ed. 1081, a corporation of Indiana sued as such, in the Circuit Court in Kentucky, a citizen of Kentucky. The defendant pleaded to the jurisdiction. The court said:

"But a decision of the question whether the plaintiff was or was not a corporation of Kentucky does not appear to this court to be required for the disposition of this case, either as to the jurisdiction or as to the merits. As to jurisdiction, it being clear that the plaintiff was first created a corporation of the state of Indiana, even if it was afterwards created a corporation of the state of Kentucky also, it was and remained, for the purposes of the jurisdiction of the courts of the United States, a citizen of Indiana, the state by

which it was originally created. It could neither have brought suit as a corporation of both states against a corporation or other citizen of either state, nor could it have sued or been sued as a corporation of Kentucky, in any court of the United States."

In other words, the Supreme Court has held that an organization may for some purposes be incorporated in a given state, and yet may not be a corporation of that state for purposes of jurisdiction. A corporation of the second class, though in some respects treated as a corporation of several states, yet remains for jurisdictional purposes a citizen of the state which originally created it, and of that state alone. Plainly, the railroads in the two cases last mentioned were of the second class, and the language just quoted is in accord with that used in *R. R. v. Harris*, 12 Wall. 65, 82, 20 L. ed. 354, 358:

"Nor do we see any reason why one state may not make a corporation of another state, as there organized and conducted, a corporation of its own, quo ad hoc any property within its territorial jurisdiction."

It cannot be supposed that the language of the court in these cases was intended to deny the existence of corporations of the first class, although, in the latest case, the Supreme Court was disposed to treat interstate railroads as corporations of the second class, where the classification was open to doubt. *Southern R. R. v. Allison*, 23 Sup. Ct. 713, 47 L. ed. 1078.

In *Memphis R. R. Co. v. Alabama*, 107 U. S. 581, 2 Sup. Ct. 432, 27 L. ed. 518, the Supreme Court held that the railroad, a corporation of the first class—that is to say, a corporation for jurisdictional purposes both of Alabama and Tennessee—could not remove into the Circuit Court in Alabama a suit brought against it by a citizen of that state. In that case it was said:

"The defendant, being a corporation of the state of Alabama, has no existence in this state as a legal entity or person, except under and by force of its incorporation by this state; and, although also incorporated in the state of Tennessee, must, as to all its doings within the state of Alabama, be considered a citizen of Alabama, which cannot sue or be sued by another citizen of Alabama in the courts of the United States." 107 U. S. 585, 2 Sup. Ct. 436, 27 L. ed. 518.

The decision was rested on *Railway Co. v. Whitton*, 13 Wall. 270, 20 L. ed. 571, and follows *Muller v. Dows*, 94 U. S. 444, 24 L. ed. 207, in both of which cases the corporation must be taken to have been of the first class. In the former case it was said:

"The defendant is a corporation, and as such a citizen of Wisconsin by the laws of that state. It is not there a corporation or a citizen of any other state. Being there sued, it can only be brought into court as a citizen of that state, whatever its status or citizenship may be elsewhere." 13 Wall. 283, 20 L. ed. 576.

If, then, a plaintiff, citizen of one state, can maintain in the fed-

eral courts in another state a suit against a corporation of the first class, created in both states (*Muller v. Dows, Railway Co. v. Whitton*), and if that corporation cannot remove into the federal court in either state a suit brought against it by a citizen of that state (*Memphis R. R. v. Ala.*), it would seem to follow that this court is without jurisdiction in the case now before it. This is certainly true if an interstate railroad of the first class is to be treated in both states and under all circumstances as one and the same corporation.

But the plaintiff urges that in the case of what has been called a corporation of the first class, such as this defendant, there are in the eye of the law two separate corporations, one having jurisdictional citizenship in Massachusetts, and one in Connecticut, and that he has chosen to sue the latter. In some of the cases cited there is language which strongly states the separate existence of two corporations. See *R. R. v. Vance*, 96 U. S. 450, 24 L. ed. 752; *Clark v. Barnard*, 108 U. S. 436, 452, 2 Sup. Ct. 878, 27 L. ed. 780; *Graham v. B. H. & E. R. R.*, 118 U. S. 161, 169, 6 Sup. Ct. 1009, 30 L. ed. 196.

In order to sustain its plea to the jurisdiction, the defendant may not be obliged to prove that a corporation of the first class is to be deemed jurisdictionally a single corporation having two aspects, in Massachusetts a citizen of Massachusetts, and in Connecticut a citizen of Connecticut. It will also prevail if it can prove that such an organization is to be deemed two separate corporations indissolubly connected, owners in common of the corporate property, each of which, in the state where created, is recognized as the owner of the property situated in both states, and in the other state is wholly ignored. Thus in *Ohio R. R. v. Wheeler*, 1 Black, 286, 297, 17 L. ed. 130, the court said:

"It is true that a corporation by the name and style of the plaintiffs appears to have been chartered by the states of Indiana and Ohio, clothed with the same capacities and powers, and intended to accomplish the same objects, and it is spoken of in the laws of the states as one corporate body, exercising the same powers and fulfilling the same duties in both states. Yet it has no legal existence in either state, except by the law of the state. And neither state could confer on it a corporate existence in the other, nor add to or diminish the powers to be there exercised. It may, indeed, be composed of and represent, under the corporate name, the same natural persons. But the legal entity or person which exists by force of law can have no existence beyond the limits of the state or sovereignty which brings it into life and endows it with its faculties and powers."

It is not true without qualification that a corporation created by one state has no existence outside that state. Corporations created outside Massachusetts sue and are sued in the state and federal courts of Massachusetts every day, and their existence is thus recognized. In the case of corporations like this defendant, however,

it may be that the Massachusetts creation alone is recognized in Massachusetts, and the Connecticut creation alone in Connecticut. See the language already quoted from *Ohio R. R. v. Wheeler*, and *Railroad Co. v. Whitton*. Whether the New York, New Haven & Hartford Railroad be considered one corporation with two aspects, or two separate corporations, a decision in favor of this plaintiff which would allow a citizen of Massachusetts to sue in this court the New York, New Haven & Hartford Railroad by styling it a corporation of Connecticut, and, by parity of reasoning, would allow the railroad, by styling itself a corporation of Connecticut, to sue a citizen of Massachusetts in this court, would ignore the railroad's real organization, and would make decisions in *Ohio R. R. v. Wheeler* and other considered cases practically ineffective, so far as a plaintiff is concerned.

In *Railroad Co. v. Vance*, 96 U. S. 450, 24 L. ed. 752, the plaintiff, the Indianapolis & St. Louis Railroad Co., was a corporation of the first class (see *Gerling v. Railroad Co.*, 151 U. S. 677, 14 Sup. Ct. 533, 38 L. ed. 311; *Pennsylvania R. Co. v. St. L., A. & T. R. Co.*, 118 U. S. 298, 6 Sup. Ct. 1094, 30 L. ed. 83), incorporated in Illinois and Indiana. Alleging itself to be a corporation of Indiana, it brought suit in the Circuit Court of Illinois to restrain the collection of taxes by a citizen of that state. If the corporation was to be deemed a citizen of Illinois, and in the federal courts of Illinois as a corporation solely of Illinois, the bill should have been dismissed for want of jurisdiction. The court entertained the bill, but dismissed it on the merits, holding that the corporation really taxed was the corporation of Illinois, and so the Indiana corporation had no cause of complaint. As the question of jurisdiction was not argued, and as the matter was not discussed or referred to in the opinion, the authority of the case in favor of the plaintiff is not great.

The plaintiff relies principally upon *Nashua & Lowell Railroad Corp. v. Boston & Lowell Railroad Corp.*, 136 U. S. 356, 10 Sup. Ct. 1004, 34 L. ed. 363.

(The learned judge proceeded to distinguish this case.)

Most of the cases decided in the state courts which deal with the status of corporations of the first class are concerned altogether with taxation or with the rights of the several states to control the operation of the railroad within their borders. This right is admitted, even as to corporations of the second class acting in states where their incorporation gives no jurisdictional status, and a fortiori is effective as to corporations of the first class in states where their incorporation does give them such status. In *Tourville v. Wabash R.*, 148 Mo. 614, 50 S. W. 300, 71 Am. St. Rep. 650, the railroad defendant was apparently a corporation of the first class. It had been garnished in Illinois, and tried to set up its payment under the judgment there rendered in defense of an action brought in Missouri by its employe and original creditor, a citizen of that state. The court said:

"So that in the defendant we have two legal entities—one a corporation and citizen of Illinois, the other a corporation and citizen of Missouri. With the former the plaintiff had no dealings, and it owed him nothing. The latter became indebted to him in the sum of \$81 for wages earned in Missouri, and under the law thereof exempt from attachment, execution and garnishment; and, while it may be difficult to see how this debt due the plaintiff from the Wabash Railroad Company of Missouri could be impounded in the courts of Illinois by the service of garnishment process on the Wabash Railroad Company of Illinois, the ruling of the Court of Appeals was not based upon the ground that it was not so subject."

The language illustrates the confusion into which the court fell in attempting to work out logically the corporate fiction. Being earned in Missouri, the plaintiff's wages were held not to have been paid by the payment made by the Illinois corporation. The Illinois court, on the other hand, seems to have deemed that the Illinois corporation also was indebted to the plaintiff, and so the corporation or corporations "a corporate trinity," or "separate corporations," paid out twice the number of material dollars actually owed. At that point the fiction failed to correspond to the facts.

Throughout the discussion we must bear in mind that we are dealing with fictions, and not with concrete facts. Corporate personality and existence are themselves fictions, and the citizenship or locality of a corporation is the fiction of a fiction. As developed by the federal courts, the citizenship of a corporation rests upon a conclusive presumption, which in hardly any case corresponds to the facts. In a corporation formed by consolidation there is but one line of railroad, of which one individual is president, and one other individual general manager. One set of individual directors sits around one table. Whether the organization is deemed (1) a single corporation, (2) one corporation with several aspects, (3) several separate corporations of which only one is recognized in each of the creating states, or (4) several separate corporations each recognized everywhere, is of no importance, except for the practical results which follow the adoption of one fiction or another. If the fourth fiction be selected, any corporation of the first class can sue or be sued in the federal court of any state by proper designation. If this result be desirable that fiction is the best for jurisdictional purposes, but care must be taken to develop the fiction so as to avoid the unjust results of the Missouri case. It is not a question of justice, but of ultimate convenience, in what court a corporation may sue and be sued; it is injustice, and not mere inconvenience, that an organization of any kind shall be compelled to pay its debts twice over. In selecting a fiction, moreover, it may sometimes be wise to take one which has some slight inconveniences in practical results, if its logical development is generally convenient, rather than another which has a slight advantage in some respect, but whose logical development would lead to such injustice that exceptions and

subfictions must be numerous and strained. If the fourth fiction above mentioned be adopted, then it must be developed so as to permit any one of the several corporations, as plaintiff or defendant, to stand for and represent them all, and the satisfaction of a judgment recovered by or against one of them must bar the collection of the same by or against any other.

In the case at bar the court has to determine what sort of fiction is applicable to the defendant for the purposes of the jurisdiction of the federal courts. Upon the whole, that fiction which treats a corporation of the first class, so-called, as one corporation with several aspects, seems to me in best agreement with the concrete facts, and the logical development of that fiction appears to produce the most convenient result. By this fiction, an organization like the defendant, maintaining a single system of railroad in many states, and chartered by each of those states so as to make it jurisdictionally a citizen of each of the states, is deemed to be one corporation, treated in each of the incorporating states as a citizen of that state and of that state alone, however it may be described in some foreign state where it has no incorporation. This theory is supported by one or two recent decisions of one Circuit Court of Appeals, and by two decisions of two Circuit Courts. For the reasons already stated, the Nashua & Lowell Case is not deemed in point, and the reasoning of the Circuit Court of Appeals in the Louisville Case and of the Circuit Court in 9 Biss. 144, Fed. Cas. No. 12,237, is shown to have been doubted by the Supreme Court on appeal.

*The plea to the jurisdiction is sustained.**

PATCH v. WABASH RAILROAD CO.

1907. 207 U. S. 277, 52 L. ed. 204.⁴

MR. JUSTICE HOLMES delivered the opinion of the court.

THIS was an action brought by the plaintiff in error to recover for the death of his intestate in a collision upon the defendant's railroad in Illinois. The action was begun in a court of the State and the defendants forthwith filed a petition for the removal of the cause to the United States Circuit Court. The petition averred, among other things, that the defendant was a corporation organized under

* *Horne v. Boston & M. R. R.* (1883) 18 Fed. 50; *Baldwin v. Chicago &c. R. Co.* (1898) 86 Fed. 167; *Smith v. New York &c. R. Co.* (1899) 96 Fed. 504; *Goodwin v. Boston & M. R. R.* (1904) 127 Fed. 986, *Accord.* *St. Louis &c. R. Co. v. Indianapolis &c. R. Co.* (1879) 9 Biss. 144, Fed. Cas. No. 12,237; *Stephens v. St. Louis &c. R. Co.* (1891) 47 Fed. 530, *contra.*

See also *St. Louis &c. R. Co. v. James* (1895) 161 U. S. 545; *Southern Ry. Co. v. Allison* (1902) 190 U. S. 326, reversing *Allison v. Southern Ry. Co.* (1901) 129 N. C. 336, 40 S. E. 91, and overruling *Debnam v. Southern &c. Tel. Co.* (1900) 126 N. C. 831, 36 S. E. 269.—Eds.

⁴Portion of opinion omitted.—Eds.

the laws of Ohio and a citizen of that State, and was not a resident of Illinois, and that the plaintiff was a citizen and resident of Illinois. The removal was ordered and completed. Thereupon the plaintiff filed in the United States Courts a plea, in which he alleged that the defendant was a corporation organized and existing under and by virtue of the laws of Illinois, Missouri, Indiana, Michigan and Ohio, by the consolidation of five other corporations severally created by the laws of those States respectively, that the defendant was a citizen of and resident in Illinois and each of said other States, and that the plaintiff was a citizen of Ohio; and the plaintiff prayed judgment whether the court could take cognizance of the action.

The defendant, after having pleaded the general issue to the action, demurred to the plaintiff's plea. Upon a hearing the demurrer was sustained, and the plaintiff electing to stand by his plea, a judgment was entered that the defendant recover its costs. The plaintiff prayed a writ of error, and the Judge certified that the judgment was based solely on the ground that the controversy was one between citizens of different States, that in his opinion the record showed that the defendant was not a citizen of or resident in Illinois, that no other ground of jurisdiction appeared, and that jurisdiction was retained only for the reasons stated. * * *

We proceed then to deal with the merits of the plea. The original certificate declares that the record shows that the defendant is not a citizen of or resident in the State of Illinois. If this be correct, it maintains the right to remove, so far as it goes. The right is given in cases of this sort to defendants "being non-residents of that State," that is, of the State in which the suit is brought. Act of August 13, 1888, c. 866, 25 Stat. 433, 434. If the defendant is to be regarded as a citizen of Illinois, the right to remove did not exist. *Martin v. Snyder*, 148 U. S. 663. It was for this reason, no doubt, that the petition for removal alleged that the defendant was a citizen of Ohio, and that the certificate declared that it was not a citizen of Illinois. But the plea averred that it was organized and existed under the laws of that State as well as of the others named. It is true, however, that it did not and could not traverse the averment of the petition, considered as an averment of fact, and it was demurred to specially on that ground. Therefore the question is raised how a corporation or corporations thus organized shall be regarded for the purposes of a suit like this. No nice speculation as to whether the corporation is one or many, and no details as to the particulars of the consolidation, are needed for an answer. The defendant exists in Illinois by virtue of the laws of Illinois. It is alleged to have incurred a liability under the laws of the same State, and is sued in that State. It cannot escape the jurisdiction by the fact that it is incorporated elsewhere. The assent of the State to such incorporation elsewhere, supposing it to have been given, a matter upon which we express no opinion, cannot be presumed to have intended or to

import such a change. This seems to be the opinion of the Supreme Court of Illinois, as it certainly has been shown to be that of this court. *Chicago &c. Ry. Co. v. Whitton*, 13 Wall. (U. S.) 270; *Muller v. Dows*, 94 U. S. 444; *Memphis &c. R. R. Co. v. Alabama*, 107 U. S. 581; *Quincy Railroad Bridge Co. v. County*, 88 Illinois, 615; *Winn v. Wabash R. Co.*, 118 Fed. 55. What would be the law in case of a suit brought in Illinois upon a cause of action which arose in Ohio is a question that may be left to one side, as also may be the decisions in cases where a corporation originally created in one State afterwards becomes compulsorily a corporation of another State for some purposes in order to extend its powers. *Southern Ry. Co. v. Allison*, 190 U. S. 326; *St. Louis &c. Ry. Co. v. James*, 161 U. S. 545. In the case at bar the incorporations must be taken to have been substantially simultaneous and free. See *Memphis &c. R. R. Co. v. Alabama*, 107 U. S. 581. If any distinction were to be made it hardly could be adverse to the jurisdiction of Illinois, in view of the requirements of its constitution and statutes that a majority of the directors should be residents of Illinois, and that the corporation should keep a general office in that State. We are of opinion that the defendant must be regarded in this suit as a citizen of Illinois, and therefore as having had no right to remove. It follows that the cause should be remanded to the state court.

*Judgment reversed.*⁵

⁵ See article, *Corporations of Two States*, by Joseph H. Beale, Jr., in 4 *Columbia Law Rev.* 391.

In *Southern R. Co. v. Allison* (1902) 190 U. S. 326, at page 335, Mr. Justice Peckham, referring to *St. Louis etc. R. Co. v. James* (1895) 161 U. S. 545, said: "Here was a corporation originally incorporated in the State of Missouri going into the State of Arkansas and operating a railroad in that State by leasing a portion of it therein and complying with a statute which provided that, upon filing a copy of its articles of incorporation with the Secretary of State of Arkansas, it should be regarded as formally incorporated in that State, and should thereby become a domestic corporation, and yet it was held that defendant could not be sued by a citizen of Missouri in the Federal court in the State of Arkansas; that although to some extent and for some purposes it might be regarded as a corporation of Arkansas, it was for purposes of jurisdiction in the Federal courts to be regarded as a corporation of the State of Missouri. The case, it will be seen, was not decided upon the ground that the cause of action had arisen in the State of Missouri. It was admitted that the cause of action was transitory, but the broad question was decided that the company was a corporation of Missouri and a citizen of that State, and could not be sued by another citizen of that state in the Federal courts of Arkansas." See also, *Missouri Pacific R. Co. v. Castle* (1911) 224 U. S. 541, p. 546.—Eds.

CHAPTER III.

CORPORATIONS DE FACTO.

METHODIST ETC. CHURCH v. PICKETT.

1859. 19 N. Y. 482.¹

SELDEN, J.—The answer in this case having denied that the plaintiffs were ever incorporated as alleged in their complaint, it was incumbent upon them to prove their incorporation upon the trial. The defendant's counsel insists that the certificate introduced for that purpose, was insufficient to support the issue on the part of the plaintiffs; because the act for the incorporation of religious societies, requires certain preliminary acts in order to incorporate under it, which acts, being virtually conditions precedent to the creation of such a corporation must be proved before its existence can be established. * * *

But a rule so inconvenient as that contended for by the defendant's counsel, has never yet been established in regard to any class of corporations. On the contrary, it has been repeatedly held, that as against all persons who have entered into contracts with bodies assuming to act in a corporate capacity, it is sufficient for such bodies to show themselves to be corporations *de facto*. This cannot be done by simply showing that they have acted as corporations for any period of time, however long. Two things are necessary to be shown, in order to establish the existence of a corporation *de facto*, viz.: 1. The existence of a charter, or some law under which a corporation with the powers assumed might lawfully be created; and, 2. A user by the party to the suit, of the rights claimed to be conferred by such charter or law. (United States Bank v. Stearns, 15 Wend. 314.)

The rule established by law as well as by reason is, that parties recognizing the existence of corporations by dealing with them, have no right to object to any irregularity in their organization or any subsequent abuse of their powers, not connected with such dealing. As long as these are overlooked or tolerated by the State, it is not for individuals to call them in question. In the case of Trustees of Vernon Society v. Hills, (6 Cow. 23), which was an action brought by the trustees of a religious corporation, Savage, Ch. J., used the following language: "The plaintiffs have acted as trustees upon the matter in question, and in bringing their suit, *colore officii*; and before an objection to their right can be sustained by the defendant, on the ground that they were not regularly elected, he must show that

¹ Only a part of the opinion is given.—Eds.

proceedings have been instituted against them by the government, and carried on to a judgment of ouster." And in the case of *Brouwer v. Appleby*, (1 Sandf. 158), in the Superior Court of the city of New York, an action brought by the receiver of a corporation upon a promissory note, and where the defense was that the corporation was never duly organized, Oakley, Ch. J., said: "The defendant, as a contracting party with this corporation, cannot object to the want of the requisite organization; and any defect in that respect, if valid, is only available in behalf of the sovereign power of the State." (*Eaton v. Aspinwall*, 19 N. Y. 119). I have said that a party to a suit, in order to show itself to be a corporation *de facto*, must prove the existence of a law authorizing its incorporation—that is, it must appear that such authority exists—if by special charter it must be proved; but when there is a general law of our own State, authorizing a particular class of incorporations, the courts, I think, will take judicial notice of it. If, however, it were otherwise, it is to be inferred that the statute authorizing the incorporation of religious societies was introduced upon the trial, as it was referred to, and relied upon by the counsel upon both sides.

But it is insisted by the defendant's counsel that there was no proof of user. The degree of proof required on this subject depends to some extent upon the nature of the incorporation, and the law under which it is organized. Where no provision is made for any permanent evidence of the fact of organization, more proof of user would be necessary than where, as in this case, the essential steps by which the organization is accomplished are required to be made a matter of record.

In such cases, if the record is perfect, then perhaps nothing else need be shown; but if imperfect, it may still stand in place of, and be equivalent to, a very considerable degree of evidence of user. The imperfection of the record cannot be taken advantage of by a private individual, who has entered into engagements with the corporation.

The rightfulness of its existence not being in issue, of course evidence of any irregularities or defects in its organization, short of such as would show a want of good faith on the part of those concerned in the proceedings, would be wholly irrelevant. If the law exists, and the record exhibits a *bona fide* attempt to organize under it, very slight evidence of user beyond this, is all that can be required.

BERGERON v. HOBBS.

1897. 96 Wis. 641, 71 N. W. 1056.

APPEAL from a judgment of the circuit court for Bayfield county:
JOHN K. PARISH, Circuit Judge. *Affirmed*.

The defendants, under the name of Bayfield Agricultural Association, employed several persons to perform labor in improving their

grounds and in erecting fences and buildings. Time checks given by the defendants to such laborers, for such labor, were assigned to the plaintiff, who brings this action to recover their amount, alleging that the defendants were a copartnership. The defendants alleged that they were members of a corporation, and denied that they were copartners, or liable as such. This was the issue which was tried. It appeared upon the trial that articles of organization of the defendants as the Bayfield County Agricultural Association, and a certificate showing the election of officers, had been recorded in the office of the register of deeds of Bayfield County, but were not on file there. They had been deposited with instruction to record and return them, which had been complied with. When the testimony of both sides was in, the court directed a verdict for the plaintiff for the amount of the time checks. From a judgment on that verdict the defendants appeal.

NEWMAN, J.—There are two questions raised on this appeal: (1) Was the mere recording of the articles of incorporation, with the certificate of the election of officers, without the intention or fact of the papers themselves remaining in the office, a sufficient compliance with the statute, so that the organization of the corporation became complete, as upon a proper filing of the papers themselves? And (2) if the recording was not sufficient for that purpose, are the defendants liable to the plaintiff only as a de facto corporation, or are they liable as copartners?

1. The statute (§ 1460, R. S.) provides that, upon the filing of "a certificate of organization * * * with a copy of the constitution," in the office of the register of deeds of the county, "such society shall have all the powers of a corporation necessary to promote the objects thereof." It cannot be doubted that the filing of the proper papers in the proper office is made, by the statute, a condition precedent to the vesting of corporate powers. The court may not be able to clearly define the respect wherein the mere recording and removal of the papers from the office fails to serve the full purpose which the legislature intended to accomplish by the filing of them. The legislature, no doubt, had good and sufficient reasons for its choice of means to promote its purpose. For the court it is not a question of equivalents. A literal filing of the papers is necessary because it is so written in the law. The term "filing" and the verb "to file," as related to this subject, include the idea that the paper is to remain in its proper order on file in the office. A paper is said to be filed when it is delivered to the proper officer, and by him received, to be kept on file. *Bouv. Law Dict.* The statute is plain and easy of observance. Valuable rights and exemption from personal liability are to be secured by its observance. It is no undue severity to require its strict observance. The defendants had not observed it, and had not secured corporate powers.

2. Had the defendants secured immunity from individual liability? No doubt, as a general rule, where an attempt to organize a corporation fails by omission of some substantial step or proceeding re-

quired by the statute, its members or stockholders are liable as partners for its acts and contracts. Beach Priv. Corp., §§ 16, 162; 1 Thomp. Corp., §§ 239, 416, 417. But the defendants' contention is that they are not within this rule, because they are at least *de facto* a corporation, and their right to be a corporation cannot be inquired into in a collateral action, but only in a direct action for that purpose by the state. The infirmity of the defendants' contention is in the assumption that they are *de facto* a corporation. In order to secure this immunity from inquiry into its right to be a corporation in a collateral action, its action, as a corporation, must be under a *color*, at least, of right. It is immaterial that they have carried on business under the supposed authority to act as a body corporate, in entire good faith. If they had not *color* or legal right, they have obtained no immunity from individual liability for the debts of the supposed corporation. (Until the articles of incorporation are filed in the office of the register of deeds of the county, there is no *color* of legal right to act as a corporation.) The filing of such paper is a condition precedent to the right to so act. So long as an act, required as a condition precedent, remains undone, no immunity from individual liability is secured. 1 Thomp. Corp., §§ 226, 508.

The defendants are not a corporation either *de jure* or *de facto*, but are liable for the plaintiff's claim as partners. It was not necessary to prove a copartnership by evidence. That was established by implication of law. Nor was it necessary to prove that the debt was unpaid. There was no presumption that it had been paid to be rebutted. The judgment of the circuit court is right, and must be affirmed.

By the Court.—*The judgment of the circuit court is affirmed.*

MARSHALL, J.—With the decision that the defendants failed to comply with all the conditions precedent to the corporate existence of the agricultural association I concur, but from the decision that because of such failure such association was not a corporation *de facto* I respectfully dissent; hence dissent from the conclusion reached that the defendants are personally liable to plaintiff, and that the judgment should be affirmed, but, on the contrary, hold that it should be reversed.

My brethren cite Beach, Priv. Corp., § 162, and 1 Thomp. Corp., §§ 239, 508, to the effect that, unless all the conditions precedent to the creation of a corporation are performed, there can be no corporation in fact, and that the members of the pretended corporation will be personally liable. Then §§ 417 and 420 of Judge Thompson's work are cited, to the effect that, if the corporation never comes into being in fact, so as to be regarded as a corporation *de facto*, the persons who have assumed to contract in its name are personally liable. These sections seem to be tied together, in the opinion of the court, as if the two ideas are in harmony, when the contrary, to my mind, is manifestly true. Thompson treats this subject in such a way as to

naturally confuse one who attempts to follow him as authority. After saying, in §§ 239, 508, in effect, that all the conditions precedent to the creation of a corporation must be complied with, in order that the members may escape personal liability, he says, in § 417, that the rule does not apply to corporations de facto, and in § 420 that where there is a corporation de facto—in other words, where the circumstances are such that a corporation might exist, and where the party seeking to charge the members individually has dealt with them as a corporation,—he is estopped from setting up the fact that they are not a corporation de jure, in order to charge them personally. From this confusion it is not to be wondered at that if a person tries to follow Judge Thompson he will be led inevitably into the position of holding that, unless all the conditions precedent to the existence of a corporation are complied with, personal liability of the members of the corporation will exist, though the rule does not apply if the organization be a corporation de facto. That comes from trying to harmonize conflicting decisions, that proceed on theories so opposite that harmony is impossible.

If we hold with Missouri, Arkansas, and some other states, that unless all the steps necessary to the creation of the corporation have been taken there is no corporate existence, and that members of the association are personally liable, we, in effect, say that it is not sufficient to enable such members to escape personal liability to show that their organization is a corporation de facto; that nothing short of a corporation de jure will do. But if we adopt the growing doctrine, supported, as I shall show, by the overwhelming weight of authority in this country, that if a person contracts with a de facto corporation, the members of the latter and such person believing, in good faith, in its legal existence, such members cannot be held personally liable, then we concede, necessarily, that it is not essential to freedom from such liability that all the statutory requisites to the existence of a corporation be complied with, because, when that is done, the organization, obviously, is not a corporation de facto only; it is a corporation de jure. This is too plain to admit of serious discussion.

While the decision in this case, as I read the opinion of the court, in one view, goes upon the ground that the members of a de facto corporation are not responsible personally, inasmuch as it may be held that the decision really is to the effect that personal liability exists because all the conditions precedent to a corporation de jure were not complied with, some reference to authorities on the subject of whether to escape such liability it is necessary that the corporation exist in fact may be proper.

The development of the law on this subject has been rapid in recent years in the direction of holding that the state only can challenge the legality of the exercise of corporate powers. The ancient doctrine was that all contracts made by a corporation in excess of its powers were void. That has not been changed, but the doctrine has

grown up and become well-nigh universal, that the state only can raise the question by proceedings to punish the corporation. Our court is fully committed to such doctrine. *John V. Farwell Co. v. Wolfe*, ante, p. 10. Following closely upon the growth of such doctrine, as applied to transactions in excess of corporate powers, where there is no question as to the existence of the corporation, it has been extended, so as to prevent private persons, who have contracted with a de facto corporation, from questioning its existence; holding that sovereign power only can raise that question. This court having fully adopted the doctrine where there is a corporation in fact, how it can be rejected where the corporation is de facto merely is not perceived, inasmuch as a controlling reason for it in the one case applies equally to the other. In both cases there is an exercise of powers that can only be lawfully exercised by sovereign authority; hence the unauthorized exercise of power constitutes a public offense, not against any individual, but against the sovereignty of the state. A few authorities of the multitude that exist on the question under discussion will be referred to.

In *Cochran v. Arnold*, 58 Pa. St. 399, the question was whether a person who had contracted with a pretended corporation, so defectively formed that in a suit by the commonwealth it would have been enjoined for want of legal existence, could, in an action against the members of such corporation to enforce personal liability, successfully question the corporate existence. The case is particularly in point here because the corporation claimed to exist by compliance with the general law, and the point was made that the rule that a private person cannot question the existence of a corporation assuming to exist under the special law does not apply fully to corporations organized under general laws. To that and the general subject Mr. Justice Strong said: "Though formed under a general law, it is, as against all the world but the commonwealth, as completely and effectually a corporate body as if it had been created by a special act of assembly and by letters patent. * * * Until the franchise claimed and used has been directly adjudged not to exist, there is a corporation de facto, at least. If there is anything settled, it is that the corporate existence of a corporation de facto cannot be inquired into collaterally. Upon this subject the authorities are too numerous to admit of citations." The learned judge then proceeds to show that the doctrine announced was contrary to earlier decisions of the court, but that happily, before any great mischiefs had been caused by the error in such earlier decisions, the opportunity was presented for correcting it and placing the court in line with the great weight of authority on the subject. Considering the consequences of a contrary view, he said, in effect: "The mischiefs of such a doctrine would be the same, whatever the mode of obtaining corporate existence. One jury might say there was no corporation; another jury find to the contrary. One creditor might sue the corporation as a valid organization; another sue the members, alleging that the charter is

null and furnishes no immunity from personal liability. New stockholders might come in, wholly ignorant of the secret vice in obtaining the corporate thing, and be held liable. The charter would have to be effective upon the one hand and ineffective upon the other. What confusion would such a monstrous doctrine produce." This language fairly expresses the idea of the court, and is not too strong to fit the case; and the ruling has been followed down to the present time by such court. In *Hamilton v. C., M. & P. R. Co.*, 144 Pa. St. 34, there was an attempt to set up want of legal incorporation, and Justice Paxton said, in effect, the corporation at least had a *de facto* existence; therefore, it could contract debts, and, if there is anything settled in the law, it is that the existence of a corporation *de facto* cannot be inquired into collaterally. See, also *Spahr v. Farmers' Bank*, 94 Pa. St. 429; also, *Guckert v. Hacke*, 159 Pa. St. 303, where the court held that though, if plaintiff had dealt with defendants as a corporation he would have been estopped from claiming against them in any other capacity, he was not in that case, because he did not know that they pretended to be a corporation; therefore, did not deal with them as such.

The same subject was treated by the Supreme Court of Georgia in *Planters' & M. Bank v. Padgett*, 69 Ga. 159, where the rule was laid down, in effect, that having contracted with the company, through its officers or agents, both parties believing the corporation to exist *de jure* as well as *de facto*, an action cannot be maintained against them personally on the contract. The members never agreed to enter into the contract severally or jointly; they never agreed to be bound as partners, or to hold themselves out as such. The contract was intended to bind the association in a corporate capacity only.

In *Gartside Coal Co. v. Maxwell*, 22 Fed. 197, the corporation was so defectively organized as to have no legal existence. An action was brought by one who had dealt with it, against the stockholders, to hold them personally liable. Judge Brewer, in delivering the opinion of the court, said, substantially, if the corporation had been challenged by the state, its exercise of corporate powers would have been enjoined, but where persons act in good faith, and suppose they are members of a valid corporation and transact business as such, and the corporate existence is not challenged by the state, they cannot be held liable as individuals; that if a person deals with a supposed corporation,—with what all persons suppose is a corporation,—he cannot afterwards turn around and say, "Well, I dealt with this supposed corporation; I thought it was a corporation; I trusted it as such; but, by reason of failure to legally incorporate, there is no legal corporation; therefore, I will hold the stockholders personally liable." I do not think that can be done. To the same effect are *Stafford Nat. Bank v. Palmer*, 47 Conn. 443; *Eaton v. Walker*, 76 Mich. 579; *Merchants' & M. Bank v. Stone*, 38 Mich. 779; *Haas v. Bank of Commerce*, 41 Neb. 757; 17 Am. & Eng. Ency.

of Law, 866, and numerous cases there cited; 4 Thomp. Corp. § 5275; Morawetz, Priv. Corp. (1st ed.), §§ 141, 142; Angell & A. Corp., § 635. In Cook, Stock, § 637, the rule is laid down and supported by many authorities, to the effect that, with few exceptions not including the case under consideration, no one is allowed to assert that the corporation was illegally incorporated until that result has been decreed by a court in a proceeding instituted for that purpose by the state; that where persons do business in good faith as a corporation, without having any legal existence as such, it is called a de facto corporation, and only the state is allowed to question its existence. So, a party contracting with such a corporation cannot defeat his obligation by saying that the corporation was never legally incorporated.

The foregoing citation of authorities has been carried to great length, but warranted, in my judgment, from the importance of the question involved. After carefully examining such authorities and the reasoning on which the doctrine discussed is based, I am unable to understand how any other conclusion can be reached than that a decision cannot be made that plaintiff in this case can attack the existence of the agricultural association as a corporation, if it were such de facto, without holding in direct conflict with the decision in John V. Farwell Co. v. Wolf, ante, p. 10, which is supported by the highest authorities in this country, and which the court certainly would not wish to question. True, there are some authorities still holding to the ancient doctrine that any one can challenge the existence of a corporation or the legality of its acts, but the trend of modern authority is to fence in, within constantly narrowing limits, the cases where private persons can attack either the existence of a corporation or the legality of its exercise of powers; and in the humble opinion of the writer, the theory that a private person can so attack a corporation will disappear altogether in the near future, either by the courts that adhere to the ancient doctrine voluntarily changing their rule on the subject, or by its being changed by statute.

Illinois has adhered as rigidly as any state to the doctrine that a creditor may raise the question of want of legal incorporation, yet, in the recent case of Winget v. Quincy B. & H. Asso., 128 Ill. 67, it was held that, if a person contracts with a corporation de facto and receives the benefit of such contract, he cannot be permitted to allege any defect in the organization of the corporation as affecting its capacity to make the contract, even if the law under which it was organized was unconstitutional; that objection to the corporate existence is available only on behalf of the sovereign power of the state. That is carrying the doctrine under discussion further than is necessary for the purposes of this case, and beyond the general rule that there cannot be a de facto corporation under an unconstitutional law, because it is absolutely necessary to the existence of a de facto corporation that there be a valid law under which it might exist de jure.

So we say the law is that he who deals with a *de facto* corporation cannot attack its legal existence, though in administering it courts do not agree as to all the reasons for the doctrine. By some it rests on the ground that courts can only enforce contracts actually made by parties—cannot make contracts for them; by others upon the ground of estoppel; by others upon the broad, universally established principle that only the state can question the existence of a corporate organization, or the legality of its exercise of powers; and by still others upon the ground that broad principles of justice and public policy require that persons who, in good faith, assume to exercise corporate powers and have a *de facto* right so to do, should not be compelled, in all their business transactions, in all courts and places, to be ready to successfully meet attacks upon their right in this regard; that so long as the law exists under which they might legally do the very thing they assume to do, and the failure to comply with the law is a mere usurpation of power, which only concerns the community in its sovereign capacity without prejudice to the individual members of the state, justice and the certainty of contracts, upon which prosperous business in the complicated, practical affairs of life depend, require that such persons as against all but the state shall be regarded as that which they assume to be, and might in fact be, except for some act on their part not attributable to bad faith. In our judgment, all of the reasons strongly support the doctrine, and either is sufficient, particularly the one sanctioned by this court in *John V. Farwell Co. v. Wolf*, ante, p. 10, that only the state can question the legality of corporate existence when there is a colorable right to so exist.

It only remains to be considered whether the association in question was a *de facto* corporation. My brethren say no, and, as I understand it, because there was a failure to perform some condition precedent to its being a corporation *de jure*. I must assume that such is really not the doctrine of this court, for the essential element of a mere corporation *de facto* is failure to comply with some provision of law requisite to its legal existence. Where such conditions are all complied with, then the corporation becomes an organization *de jure*, as well as *de facto*, and the doctrine pertaining to the latter class of official bodies has no application whatever. If it were the law that a corporation must be such *de jure* in order to be such *de facto*, obviously, the doctrine pertaining to the latter, upon which much learning has been displayed by the courts and text-writers, would stand as the result of much useless expenditure of mental energy. The true doctrine is that it is sufficient to constitute a corporation *de facto*, as against one who has recognized its corporate existence, that there be a law under which it might exist *de jure*, an attempt in good faith to organize under such law, and a subsequent user of the assumed corporate powers. This is not an open question in this state. In *Evenson v. Ellingson*, 67 Wis. 634, the question was considered, and in an opinion by Mr. Justice Orton

the rule was laid down, in effect, as above stated, and the case has been since approvingly cited by standard text-writers and by many of the highest courts of the country as a correct exposition of the law. I might rest this opinion on the subject of whether the association in question was a *de facto* corporation, upon the principle there laid down, but, inasmuch as the subject is one of considerable importance, and one which the court will be liable to consider on some future occasion, some general treatment of the subject is necessary to meet the purposes of this opinion. The transaction of business by corporate bodies has become so very general, and the system is growing so rapidly, that just what is necessary in order that persons assuming to exercise corporate powers may safely consider themselves a corporation *de facto* is of the highest importance to the safe conduct of the multitude of business operations conducted by such bodies, and to an understanding by such persons of their legal liability.

One of the earliest and best considered cases on this subject is *Methodist E. U. Church v. Pickett*, 19 N. Y. 482. The corporation claimed to exist under a general law. Such law required the making, acknowledging, and recording of a certificate of organization, showing certain facts. That was complied with, except that the certificate did not show the existence of all facts requisite to a legal corporation. After acting as a corporation for some time, in an action brought as such to which a private person was a party, its corporate existence was challenged. On the question thus presented, Mr. Justice Selden, speaking for the court, said: "It has been repeatedly held that, as against all persons who have entered into contracts with bodies assuming to act in a corporate capacity, it is sufficient for such bodies to show themselves to be corporations *de facto*, and to that end two things are necessary: (1) The existence of a charter or some law under which a corporation with the powers assumed might lawfully be created; and (2) a user by the party to the suit of the rights claimed to be conferred by such charter or law. The rule established by law, as well as by reason, is that parties recognizing the existence of corporations, by dealing with them, have no right to object to any irregularity in their organization. As long as it is overlooked or tolerated by the state, it is not for individuals to call it in question." And further, in effect, that if the law exists, and the record exhibits a bona fide attempt to organize under it, or there is even a slight evidence of user, that is all that is required to establish the corporation *de facto*; and evidence, in a contest between it and one who has dealt with it as a corporation, of defects in its organization, short of such as would show a want of good faith on the part of those concerned in the proceedings, would be wholly immaterial. Judge Selden refers to numerous earlier decisions in New York on the subject, particularly to *U. S. Bank v. Stearns*, 15 Wend. 314, *Trustees of Vernon Soc. v. Hills*, 6 Cow. 23, and *Brouwer v. Appleby*, 1 Sandf. 158, where Oakley, C. J. discussing the same

subject, said: "The defendant, as a contracting party with this corporation, cannot object to the want of the requisite organization, and any defect in that respect, if valid, is only available in behalf of the sovereign power of the state."

Vanneman v. Young, 52 N. J. Law, 403, touches the instant case at every point. The condition precedent which defendants here failed to perform was that as to filing in the office of the register of deeds their constitution and certificate of organization. They recorded their articles of organization, which were adopted, in form, under the general incorporating act, not that relating specially to agricultural societies; so that the record, speaking with reference to the papers required to be on file with the register of deeds, was not merely defective; it did not exist at all. Now it may be contended that, while such official record need not show that all the steps requisite to the organization of the corporation were taken, in order to give it colorable existence, an official record of some sort, showing an attempt to comply with the law, is necessary. In *Methodist E. U. Church v. Pickett*, *supra*, the following language is used: "If the law exists, and the record exhibits a bona fide attempt to organize under it," that is sufficient. This may be deemed to signify that the record referred to must be an official record,—the record which the law requires shall be made. The same language is used in *Angell & A. Corp.*, § 635, but a careful examination of the authorities will clearly show that the record intended is not the record of the corporation papers required by law. The word "record" refers solely to the acts shown by the evidence to have been actually done by the persons assuming to act as a corporation, by way of complying with the law authorizing its organization. Such facts constitute the record, in a legal sense, of their doings, and by such record it must appear that they, in good faith, intended to acquire corporate power.

In *Vanneman v. Young*, *supra*, there was, as here, an absolute failure to comply with the law in respect to the official record. The certificate of incorporation was not filed in the office of the secretary of state. That, under the New Jersey law, was essential to corporate existence. Plaintiff sold to the pretended corporation some merchandise, and, upon payment therefor not being made, suit was brought by him against the members of the corporation, to charge them personally as partners, upon the ground that the corporation had no legal existence. In deciding the question thus presented, Mr. Justice Dixon said, in effect: "The statute authorized the incorporation of the associates. They attempted to organize under its provisions. The contract was entered into by plaintiff on the assumption that he was dealing with a corporation *de jure*. The failure of the associates to comply with the statute did not, in the least, impair the rights which the plaintiff intended to secure by his contract. Under these circumstances, the plaintiff cannot bring into question the legality of the corporation. Where the law authorizes a corporation,

and there is an effort in good faith to organize under the law, and, as a result of such effort, corporate functions are assumed and exercised, the organization becomes a corporation de facto, * * * and its existence can only be inquired into in a direct proceeding brought in the name of the state. No private person having dealings with a de facto corporation can be permitted to say that it is not a corporation de jure."

In *Georgia S. & F. R. Co. v. Mercantile T. & D. Co.*, 94 Ga. 309, there was a general law under which the organization might have been incorporated. It organized under a special law that was held unconstitutional. There was an entire absence, it will be observed, of any official record of any act done under the general law. It was held that the special law was unconstitutional and void; hence that the organization had no de jure existence; nevertheless, that it was a corporation de facto; that the essentials of a de facto corporation were all present: (1) A law under which the organization might have been incorporated; (2) a bona fide attempt to become incorporated; and (3) an assumption and exercise of the powers of a corporation, unchallenged by the state.

The foregoing authorities are believed to fairly state the law in respect to what is necessary to constitute a corporation de facto. The very meaning of the term "de facto" indicates that nothing more is necessary to the existence of a de facto corporation than the exercise of corporate powers in good faith. Corporation de facto,—that is, a corporation from the fact that it is acting as such under color of right in good faith. The existence of the law, and some attempt to comply with it, are essential, because without them there can be no assumption of the right to corporate existence in good faith. Persons cannot be said to honestly claim the right to corporate existence, in the absence of any law authorizing the organization, or in the absence of some honest attempt to comply with such law, if one exists. The law and such attempt, or user of the franchise, whatever mistakes may be made in so doing,—such as the filing of articles of organization when they are required to be recorded, or the recording of articles when they are required to be filed, or the filing of such articles in the wrong office, or any other of the numerous mistakes that might be made,—make a corporation good everywhere, in all courts and places, till successfully challenged by the state. There is hardly any end of authority, all in harmony on this subject, but we content ourselves by referring to the following additional cases: *Haas v. Bank of Commerce*, 41 Neb. 754; *East Norway Lake N. E. L. Church v. Froislie*, 37 Minn. 447; *Snider's Sons' Co. v. Troy*, 91 Ala. 224; *Stout v. Zulick*, 48 N. J. Law, 601; *McCarthy v. Lavasche*, 89 Ill. 270; *Hudson v. Green Hill Seminary Corp.*, 113 Ill. 618; *St. Louis v. Shields*, 62 Mo. 247; *Central A. & M. Asso. v. Alabama G. L. Ins. Co.*, 70 Ala. 120; *Palmer v. Lawrence*, 3 Sandf. 161; *North v. State ex rel. Pate*, 107 Ind. 356.

From the foregoing, I am warranted in asserting that, by well-settled principles of law, the agricultural association with whom plaintiff contracted was a *de facto* corporation. Every element necessary to make it such appears clearly by the record. There was a law under which it might have existed. The association prepared their constitution, and adopted it in the form of ordinary articles of organization, under the general incorporating act, and by mistake they filed it for record, and it was recorded and returned, instead of filing it to be left in the office, as the law requires. They supposed that they had corporate existence by reason of the recording of their articles of organization. They assumed to act as a corporation, and exercised corporate powers for a considerable length of time, and, for aught that appears, in the utmost good faith. Certainly, the existence of the law, the making and recording of articles of organization in an honest attempt to become a corporation, and the honest assumption and exercise of corporate powers, *prima facie*, establishes good faith. Plaintiff supposed that the corporation was a corporate body till long after his contract relations with the association ceased. Now to allow him to come in and say that the corporation did not exist which all supposed had legal existence; that, though the officers of the association and plaintiff contracted for a corporate liability on the part of the former, it shall be held, nevertheless, that the members of such association are bound as partners, in direct violation of the well-settled law that such an association, under the circumstances, was a *de facto* corporate body, and that, as between the parties, the relations are the same in all respects as though the corporation had a *de jure* existence, and contrary to the settled doctrine, as I believe, of this and most other courts,—is what the judgment in this case does, in my opinion.

I think the judgment of the circuit court, holding the defendants liable as partners, was wrong, and that it should be reversed, and the cause remanded for a new trial.

NEWCOMB-ENDICOTT CO. v. FEE.

1911. 167 Mich. 574, 133 N. W. 540.

ASSUMPSIT in justice's court by Newcomb-Endicott Company against Robert L. Fee and others for goods sold and delivered. Plaintiff recovered and defendants appealed to the circuit court. A judgment for defendants on verdict directed by the court is reviewed by plaintiff on writ of error. Affirmed.

STONE, J.—This case originated in justice's court, where the plaintiff recovered a judgment, and the defendants appealed to the circuit court.

In the first count of the declaration the defendants are sued as

copartners, doing business as Fred J. Pound Company. It is alleged that they were indebted to the plaintiff for the price and value of a bill of goods amounting to \$117.90, sold and delivered to the defendants by the plaintiff.

The second count alleges that the Fred J. Pound Company was a corporation organized and existing under the laws of the state of Michigan, and was indebted to the plaintiff in the above sum for goods sold and delivered to the said Fred J. Pound Company. It is further alleged that the defendants were directors of said corporation during the months of January and February in the year 1909, and during the first 10 days of the month of March, 1909; that it became the duty of such directors, in accordance with the statute, during the months of January and February, and during the first 10 days of the month of March, 1909, to join in the making of an annual report of the affairs of the Fred J. Pound Co., the said corporation. It is further alleged that the defendants, well knowing their duty in this behalf neglected and refused to join in the making of such report during the time above alleged, and continued to so neglect and refuse to join in the making of such report until the 31st day of March, 1909, when the report was made; and the plaintiff alleges, that in accordance with said statute, said defendants became and were liable for all the debts of the said corporation, and especially for the debt aforesaid, incurred in the month of July, 1908, to which declaration is added the common counts in assumpsit.

Upon the trial of the case in the circuit court, William H. Anderson was produced as a witness for the plaintiff, and testified that during the years of 1908 and 1909 he was the bookkeeper of the plaintiff, and that the goods sued for were installed in Pound & Co.'s Inn. He did not know who ordered them; witness was not the selling party; that he extended the credit to Pound & Co. in June and July, 1908; that he knew that the defendant Fee was connected with the company. Witness was not familiar with the form of the organization of the company. He did not know whether it was a corporation or a partnership. Defendant's counsel, when asked if he would admit the amount of the bill, answered as follows:

"We cannot deny it. We will have to admit it. We will show Mr. Pound bought them, and we suppose it is all right."

It appeared that the bill had never been paid. On cross-examination the witness testified that he had no personal knowledge what individual bought the goods; that he was asked for credit for the F. J. Pound Co. by someone, and he extended credit to the F. J. Pound Co. Witness did not go to the county clerk's office to find out whether Pound & Co. had filed their articles of association or not. Witness testified that the plaintiff sent statements every two or three months to F. J. Pound & Co. The plaintiff, on re-examination of the witness, offered in evidence the articles of association of the F. J. Pound Company. The articles show that the three defendants, as incorporators, desiring to become incorporated under the provi-

sions of Act No. 232 Pub. Acts 1903, known as the "Manufacturing & Mercantile Act," executed and adopted the articles of association in due form. The articles were signed by the three defendants, and duly acknowledged on the 5th of June, 1908, before a notary public. It appears that the articles of association were filed with the secretary of state June 15, 1908, and duly recorded, and that they were filed with the county clerk on March 22, 1909. There was no evidence that the defendants had attempted to carry on a business as copartners prior to the execution of the articles above referred to.

Defendant Fee testified that he was president and stockholder of the F. J. Pound Company; that he recollected when the articles of association were executed, and signed the articles; that he supposed they were duly filed, and that he left them with Mr. Bock to be filed; that Mr. Bock was one of the directors. Defendant Bock testified that the articles were duly executed, that they were sent to the secretary of state; that, when they came back, they were copied in the secretary's record book; that the articles were filed with the county clerk sometime in March, 1909; that Mr. Pound was the manager of the said company.

At the close of the testimony counsel for plaintiff made a motion to direct a verdict for the plaintiff, for the reason that the articles of association were not filed in accordance with the statute of the state of Michigan, providing that a corporation shall transact no business until its articles of association have been filed in the office of the secretary of state and with the clerk of the county where the corporation has its principal office—in both places; that the undisputed testimony shows that the articles were filed in the office of the secretary of state June 15, 1908; that the bill for which this suit is brought was contracted in July, 1908, and the articles of association were not filed in the office of the county clerk until March, 1909; and that in the meantime the corporation did carry on business in violation of the statute, and that these defendants should be held as copartners.

That the trial judge held that the corporation was a de facto corporation when the articles were filed in the office of the secretary of state, that the corporation de facto was in existence at the time the credit was extended, and that the credit was extended to the company, and not to the individuals. In his charge to the jury the trial judge used the following language:

"The plaintiff alleges that the copartnership was in existence by reason of their not having filed articles of incorporation in the office of the county clerk until after the credit had been extended. The undisputed testimony shows that the gentlemen named signed articles on the 5th day of June, and that on the 15th day of June those articles were filed with the secretary of state at Lansing. After that time, in the month of July, that year, credit was extended by the Newcomb-Endicott Company to Fred J. Pound Company upon their books as shown in the testimony. I believe that the testimony shows that credit was extended, not to the various defendants individually,

but to Fred J. Pound Company. While it possibly may be that the company had not fully completed all of the requisites of incorporation, and had not filed their articles in the county clerk's office, still I charge you that they were at the time a corporation de facto under the laws of the state of Michigan, as I understand them, and a person dealing with a corporation de facto is estopped from denying its validity. I charge you that this suit should have been brought for these goods against the Fred J. Pound Company, a body corporate. Your verdict should be for the defendants, no cause of action."

A verdict was thereupon returned for the defendants, and the judgment followed.

The plaintiff has brought the suit here by writ of error, and the errors relied upon by the appellant in the brief of counsel are:

(3) That the court erred in denying the motion of plaintiff's counsel, at the close of all the evidence, to direct a verdict for the plaintiff, for the reason that the defendants, not having complied with the statute of the state of Michigan in regard to filing the articles of association in the office of the county clerk of Wayne county, were not entitled to carry on business as a corporation, and were copartners at the time the articles mentioned in the bill of particulars were purchased.

(4) That the court erred in holding that a corporation de facto was in existence at the time credit was extended, and that credit was extended, not to the individuals composing Pound & Co., but to the de facto corporation.

(5) That the court erred in directing the jury to return a verdict for defendants of no cause of action.

Counsel for plaintiff in his brief says that the only question involved is whether the plaintiff can hold defendants liable as partners for the goods purchased before they had recorded their articles of association with the county clerk. It is the claim of plaintiff's counsel that recording the articles of association is a prerequisite to corporate existence. The act in question provides as follows:

"Before any corporation, organized under this act to operate in this state shall commence business, the president shall cause the articles of association to be recorded at the expense of said corporation in the office of the secretary of state of this state, and in the office of the county clerk in which such operations are to be carried on."

(Act No. 232, § 9, Pub. Acts 1903.)

The plaintiff insists that this prohibits business dealings in the corporate name, and under corporate liability until the conditions therein specified, i. e., the filing of the articles both with the secretary of state and the county clerk, had been fulfilled. He cites in support of this proposition *Whipple v. Parker*, 29 Mich. 369. In that case Justice Christiancy, who spoke for the court, said, on page 379:

"But there was no proof of the filing of the articles with the secretary of state, as required of corporations of this kind before they

are allowed to commence business. Comp. Laws 1871, § 2838. And it was probably for this reason (for the record does not show the ground) that the objection was made that there was no legal evidence of incorporation. But whether this statute does not recognize the corporation as in existence before the filing of the articles, and whether the want of such filing before commencing business is not an objection which can only be made on behalf of the state, as we are inclined to think; or whether the defendant as a member, participating in the formation and in the business of this corporation de facto, was not estopped from denying its incorporation (*Swartwout v. Railroad Co.*, 24 Mich. 389), and whether there was not legal evidence of the corporation, are questions not necessary to the decision of this case, and I do not propose to consider them."

In 10 Cyc. p. 253, we find the following:

"A corporation de facto exists when there is: (1) A charter or statute under which a corporation with the powers assumed might have been organized. (2) A bona fide attempt to organize a corporation under such a charter or statute. (3) An actual user of the corporate powers or some of them which might have been rightfully used by such an organization. Such being the proper conception of a corporation de facto, it follows that a substantial compliance with the law in effecting a corporate organization is not necessary to constitute the body a corporation de facto, because that makes it a corporation de jure."

It will be noted that there is no claim in this case that the plaintiff extended credit to the defendants as co-partners, because the witness Anderson distinctly testified that he was not familiar with the form of the organization or company, and that he did not know whether it was a corporation or a partnership. There is no evidence that prior to the attempted incorporation the defendants ever did business as co-partners, or jointly in any manner. In the case of *Whitney v. Wyman*, 101 U. S. 392, a Michigan statute similar to the one in question was before that court. In that case the corporation was organized under the statute of this State, which authorized mining and manufacturing companies to be created pursuant to its provisions. There the articles had not been filed with the secretary of state, or the county clerk at the time of giving the order. They were afterwards filed in both offices. The statute declared that they should be so filed before the corporation could commence business. The court, speaking through Mr. Justice Swayne, after referring to the point made by counsel that the corporation at the date of the order was forbidden to do any business, not having then filed its articles of association as required by the statute, said:

"The restriction imposed by the statute is a simple inhibition. It did not declare that what was done should be void, nor was any penalty prescribed. No one but the State could object. The contract

is valid as to the plaintiff, and he had no right to raise the question of its invalidity."

It seems to us that the trial judge was correct in holding that the plaintiff was dealing with a corporation de facto, and it cannot be said that the plaintiff supposed that it was dealing with the co-partners, for it clearly appears that it did not know whether it was dealing with co-partners or with a corporation. In *Swartwout v. Railroad Co.*, supra, this court held that, in the case of the associates in the corporation de facto and those who have had dealings with it, there is a mutual estoppel resting upon broad grounds of right, justice, and equity, which prevents the former from denying, and the latter from disputing, the incorporation. *Johns v. People*, 25 Mich. 502.

Although the proposition finds some support in the authorities cited by counsel from other states, we cannot agree with counsel for appellant when he states that, until the recording of the articles of association with the county clerk, the Fred J. Pound Company could have no corporate existence. By the act itself it is provided that the president shall cause the articles of association to be recorded. The statute therefore contemplates the complete organization of the association and the election of officers before the recording of the articles, and we think that the better doctrine is that the State only can interfere in a case such as the one with which we are dealing.

There is no claim of fraud or false representation here. And it seems to us that it is undisputed that there was a bona fide attempt to organize a corporation under the statute. Where an attempt has been made to organize a corporation under a valid act, and the question is one of regularity merely, parties recognizing its legal corporate existence by dealing with it have no right to object to any irregularity in such organization.

As this court said in *Eaton v. Walker*, 76 Mich. 585 (43 N. W. 640 [6 L. R. A. 102]): "Two things are necessary to be shown in order to establish a corporation de facto, viz.: (1) The existence of a charter or some law under which a corporation, with the powers assumed, might lawfully be created. (2) A user by the party to the suit of the rights claimed to be conferred by such a charter or law. *U. S. Bank v. Stearns*, 15 Wend. (N. Y.) 314. If the law exists, and the record exhibits a bona fide attempt to organize under it, very slight evidence of user beyond this is all that can be required. *M. E. Church v. Pickett*, 19 N. Y. 487."

Both of these requisites appear in the instant case.

We think the trial judge was justified in directing a verdict for the defendants, and the judgment of the circuit court is *affirmed*.

OSTRANDER, C. J., and STEERE, MOORE, and BROOKE, JJ., concurred.²

² *Snider's Sons Co. v. Troy* (1890), 91 Ala. 224, 8 So. 658; *Owensboro Wagon Co. v. Bliss* (1901), 132 Ala. 253, 31 So. 81; *Tarbell v. Page* (1860), 24 Ill. 46; *Hoyt v. McCallum* (1902), 102 Ill. App. 287; *Finnegan v. Noerenberg* (1893), 52 Minn. 239, 53 N. W. 1150; *Johnson v. Okerstrom* (1897), 70

STEVENS v. EPISCOPAL CHURCH HISTORY CO.

1910. 140 App. Div. (N. Y.) 570, 125 N. Y. S. 573.¹

LAUGHLIN, J. * * * The learned counsel for the respondents contends that the execution of the certificate of incorporation constituted the defendant a corporation *de facto*. * * *

Section 5 of the former General Corporation Law (Gen. Laws, chap. 35; Laws of 1892, chap. 687), as amended by chapter 285 of the Laws of 1902, which is now section 5 of the General Corporation Law (Consol. Laws, chap. 23; Laws of 1909, chap. 28), required that the certificate of incorporation should be filed in the office of the Secretary of State, and should be by him duly recorded and indexed, and that a certified copy thereof or a duplicate original should be filed and similarly recorded and indexed in the office of the clerk of the county in which the office of the corporation was to be located, and further provided as follows: "All taxes required by law to be paid before or upon incorporation and the fees for filing and recording such certificate must be paid before filing. No corporation shall exercise any corporate powers or privileges until such taxes and fees have been paid." The execution of the certificate without any action directing or authorizing the filing thereof and without the filing thereof did not even constitute an attempt to comply with the requirements of the statute and created no liability and imposed no obligation on the parties who signed it to perfect the incorporation. At most it merely constituted an agreement among themselves, and in transacting business in the name of the corporation they doubtless became liable as copartners; but in no view of the case can it be maintained that the mere execution of the certificate created a corporation *de facto*. Of course, where there has been an attempt in good faith to comply with the requirements of the law with respect to filing a certificate of incorporation and a certificate has been filed in one or more of the places required by law and there has been user

Minn. 303, 73 N. W. 147 (repudiating *Bergeron v. Hobbs*, 96 Wis. 641, 71 N. W. 1056); *Rutherford v. Hill* (1892), 22 Ore. 218, 29 Pac. 546 (see note in 17 L. R. A. 549); *American Salt Co. v. Heidensheimer* (1891), 80 Tex. 344, 15 S. W. 1038, *Accord*.

In the following cases the shareholders of a *de facto* corporation were held not exempt from individual liability. *Garnett v. Richardson* (1879), 35 Ark. 144; *Kaiser v. Lawrence Savings Bank* (1881), 56 Iowa 104, 8 N. W. 772; *Bigelow v. Gregory* (1874), 73 Ill. 197 (partnership liability); *Loverin v. McLaughlin* (1896), 161 Ill. 417, 44 N. E. 99 (statutory provision); *Williams v. Hewitt* (1895), 47 La. Ann. 1076, 17 So. 496; *Abbott v. Omaha & Co. Refining Co.* (1876), 4 Neb. 416; *Wechselburg v. Flour City Nat. Bank* (1894), 64 Fed. 90, 12 C. C. A. 56.

As to whether there must be a dealing on a corporate basis, see *Christian & Co. v. Fruitdale Lumber Co.* (1898), 121 Ala. 340, 25 So. 566; *Doty v. Patterson* (1900), 155 Ind. 60, 56 N. E. 668; *Guckert v. Hacke* (1893), 159 Pa. St. 303, 28 Atl. 249; *Slocum v. Head* (1900), 105 Wis. 431, 81 N. W. 673; *Clausen v. Head* (1901), 110 Wis. 405, 85 N. W. 1028.—Eds.

¹ Only a portion of the opinion is given.—Eds.

of the corporate name, the corporation will be deemed a corporation *de facto*, and no one other than the people of the State can question the validity of its existence; but some of the statutory steps must be taken in an attempt to comply with the requirements of the law, and the mere execution of a paper which is not filed and does not become a public record is insufficient and this may be inquired into collaterally by any person whose interests are affected thereby. (*McLennan v. Hopkins*, 2 Kan. App. 260; *Jones v. Aspen Hardware Co.*, 21 Colo. 263; *Van Buren v. Reformed Church of Gansevoort*, 62 Barb. 495; *Lamming v. Galusha*, 81 Hun 247; *affd.*, 151 N. Y. 648; *Card v. Moore*, 68 App. Div. 327; *affd.*, 173 N. Y. 598; *Eaton v. Aspinwall*, 19 Id. 119; *Childs v. Smith*, 55 Barb. 45; *revd. on another point*, 46 N. Y. 34).⁴

MONTGOMERY v. FORBES.

1889. 148 Mass. 249, 19 N. E. 342.

CONTRACT, to recover the price of goods sold and delivered.

At the trial in the Superior Court, before *Dewey, J.*, the only question was whether the goods were sold to a corporation called the Forbes Woolen Mills, or to the defendant as doing business under that name. The plaintiffs introduced evidence tending to show that subsequently to May, 1885, they received an order for the goods by a letter, written upon paper with the printed heading, "Incorporated 1885. Forbes Woolen Mills. George E. Forbes, Treasurer," and signed, "Forbes Woolen Mills by Geo. E. Forbes, Treasurer"; that they thereupon shipped the goods to the Forbes Woolen Mills and received in payment therefor three promissory notes, together equal

⁴ *McLennan v. Hopkins* (1895), 2 Kan. App. 260, 41 Pac. 1061 (failure to prepare and file certificate); *Uteley v. Union Tool Co.* (1858), 11 Gray (Mass.) 139 (no articles entered into); *Van Buren v. Reformed Church* (1872), 62 Barb. (N. Y.) 495 (mere assumption and user); *Perrine v. Levin* (1910), 68 Misc. (N. Y.) 327, 123 N. Y. S. 1007 (certificate not filed with Secretary of State), *Accord*.

Failure to have signatures of subscribers to capital stock in the certificate as required, *Gelders v. State* (1909), 164 Ala. 592, 51 So. 232, to have the certificate signed at the end, *Lyell Ave. Lumber Co. v. Lighthouse* (1910), 137 App. Div. (N. Y.) 422, 121 N. Y. S. 802, to pay the statutory incorporation fees, *Christian & Co. Grocery Co. v. Fruitdale Lumber Co.* (1898), 121 Ala. 340, 25 So. 566; *Slocum v. Providence & Co. Pipe Co.* (1870), 10 R. I. 112; *Slocum v. Warren* (1871), 10 R. I. 116; *Hughesdale Mfg. Co. v. Vanner* (1879), 12 R. I. 491, *held*, not to prevent *de facto* corporate existence. But see *Jones v. Aspen Hardware Co.* (1895), 21 Colo. 263, 40 Pac. 457, holding payment of fees "a condition precedent to the exercise of any corporate power."

According to prevalent American doctrine, stockholders of a defectively incorporated company which is not a *de facto* corporation, are personally liable. See article by F. M. Burdick, "Are Defectively Incorporated Associations Partnerships?" in 6 *Columbia Law Rev.* 1-14.—Eds.

Failure

to the price of the goods, signed "Forbes Woolen Mills by Geo. E. Forbes, Treasurer"; that when they sold the goods and took the notes, they understood from their correspondence with the defendant, as well as from information gained from a commercial agency, that the Forbes Woolen Mills were a corporation, and made all charges on their books against them as a corporation, and took the notes from the defendant as the notes of a corporation; and that after they sold the goods and received the notes they became satisfied there was no such corporation as the Forbes Woolen Mills; and contended that they were entitled to recover the price of the goods from the defendant personally.

The defendant contended that the Forbes Woolen Mills was a corporation, and testified that he purchased the goods as treasurer of the Forbes Woolen Mills, but admitted that they had not been paid for except by the notes, which themselves had not been paid; that in May, 1885, for the purpose of limiting his personal responsibility, and because the tax laws of New Hampshire were more favorable to corporations than the Massachusetts laws, he went to Nashua, New Hampshire, to form a corporation for the manufacture of woolen goods; that he employed an attorney at law of Nashua to incorporate the company in a legal and proper manner, under the laws of that State, and subsequently paid him for his services and disbursements in the premises; that he went to Nashua again, and with the attorney and three other persons, selected and secured by the attorney, signed and executed an agreement of association, which was dated May 6, 1885, and was duly recorded in the office of the Secretary of State of New Hampshire on May 12, 1885, and in the office of the clerk of the city of Nashua on May 13, 1885, and recited that the subscribers associated themselves for the purpose of forming a corporation, to be called the Forbes Woolen Mills, the amount of the capital stock to be twenty thousand dollars, divided into four hundred shares of fifty dollars each; and that the object of the corporation was to manufacture and sell woolen and other goods, and the places of business were Nashua in New Hampshire, and East Brookfield in Massachusetts.

The defendant further testified that, subsequently to the execution of the agreement of association, one or more meetings were held by the signers, at which he was elected president and treasurer of the corporation, and such other officers and directors were elected as were necessary under the laws of New Hampshire; that the attorney had been recommended to him as a reputable and reliable man and attorney, and he left everything in his hands, and supposed he did everything necessary and proper to establish the corporation in a legal manner; that records of the meetings were kept by the attorney, and that there was a stock-book and certificates of stock were issued; that all the stock was issued to the defendant, and that no other person was interested in it; that fifty per cent of the capital stock of the corporation was actually paid in by him in cash and

supplies; that after the organization of the corporation he hired, as treasurer of the corporation, a mill in East Brookfield belonging to his mother, Roxanna Forbes, and himself, and began the manufacture of woolen goods; that he purchased the necessary supplies, including those named in the plaintiff's account, and placed them under the direction of a superintendent, employed to supervise the manufacture of the goods; that there was no manufacturing done in Nashua, nor any other business except the holding of corporate meetings, and possibly the sale now and then of a bill of goods in the ordinary course of business; and that the principal place of business of the corporation was in East Brookfield; that he, as president and treasurer of the corporation, continued to manufacture woolen goods for about four months, and sent the goods to commission houses in New York to be sold; and that at the end of said four months he was unable to continue the business and gave it up, and no further business was done by him or by the corporation.

The following sections of chapter 152 of the General Laws of New Hampshire of 1878, were introduced in evidence:

"Sect. 1. Any five or more persons of lawful age may, by written articles of agreement, associate together, for agricultural, educational, or charitable purposes, or for carrying on any lawful business, except banking and the construction and maintenance of a railroad; and when such articles have been executed and recorded in the office of the clerk of the town in which the principal business is to be carried on, and in that of the Secretary of State, they shall be a corporation, and such corporation, its officers and stockholders, shall have all the rights and powers, and be subject to all the duties and liabilities of similar corporations, their officers and stockholders, except so far as the same are limited or enlarged by this chapter.

"Sect. 2. The object for which the corporation is established, the place in which its business is to be carried on, and the amount of capital stock to be paid in, shall be distinctly set forth in its articles of agreement."

Upon this evidence, the defendant asked the judge to rule that the plaintiffs were not entitled to recover, that the account in question had been paid by the notes of the Forbes Woolen Mills as a corporation, and that there was no evidence to authorize the jury to find for the plaintiffs.

The judge declined so to rule, and submitted the following questions to the jury: "1st. Did the Forbes Woolen Mills and the members of said alleged corporation, including said Forbes, at the time of its attempted organization, intend to carry on its business as a manufacturing corporation (other than holding meetings of its members and officers) in whole or in part in the city of Nashua, New Hampshire? 2d. Was there an attempt in good faith on the part of the defendant, Forbes, to organize the corporation of the Forbes Woolen Mills? 3d. Did said Forbes, at and prior to the time the goods in controversy were ordered, namely, at all times after May

12, 1885, during his dealings with the plaintiff, believe that the organization of said Forbes Woolen Mills was a valid corporation?"

The jury answered the first two questions in the negative, and the third in the affirmative.

The judge, being of the opinion that, upon the findings of the jury and the uncontradicted evidence in the case, the plaintiffs were entitled to recover, directed the jury to return a verdict for the plaintiffs, and reported the case for the determination of this court.

C. ALLEN, J.—The apparent corporation was not a corporation. The statute of New Hampshire requires five associates, and the articles of agreement must be recorded in the town in which the principal business is to be carried on, and the place in which the business is to be carried on must be distinctly stated in the articles; otherwise there is no corporation. The defendant's pretended associates were associates only in name; he alone was interested in the enterprise. The articles of agreement were recorded in Nashua, and stated that the business was to be carried on there; but it was not in fact carried on there, and was not intended to be. The defendant took all the shares of the capital stock, and paid in to himself as treasurer only fifty per cent of the amount thereof. This is not a case where there has been a defective organization of a corporation which has a legal existence under a valid charter. Here there was no corporation. It was just the same as if the defendant had done nothing at all in the way of establishing a corporation, but had conducted his business under the name of the Forbes Woolen Mills, calling it a corporation. The business was his personal business, which he transacted under that name. *Fuller v. Hooper*, 3 Gray, 334, 341. *Bryant v. Eastman*, 7 Cush. 111.

The jury found that he did not in good faith attempt to organize the corporation, but that he believed it to be a valid corporation. His belief, in view of the facts of the case, is immaterial. Under this state of things, the defendant bought goods of the plaintiffs for his own sole benefit, adopting the name of the apparent corporation, which had no real existence, and which represented nobody but himself. He cannot escape responsibility for his purchases by the device of putting such a mere name between himself and the plaintiffs. The purchase was in substance by and for himself alone. The plaintiffs might have repudiated the transaction, and maintained replevin, if they had learned the facts in time. They may also treat the transaction as a sale to the defendant personally. *Fay v. Noble*, 7 Cush. 188, 194. *Kelner v. Baxter*, L. R. 2 C. P. 174, 183, 185. 2 Kent Com. (13th ed.) 630.

Since the notes represented nothing, the plaintiffs were at liberty to treat them as void, and recover on the original contract for goods sold. *Melledge v. Boston Iron Co.* 5 Cush. 158, 171.

*Verdict to stand.*⁵

⁵ *Booth v. Wonderly* (1873), 36 N. J. L. 250; *Gartside Coal Co. v. Maxwell* (1884), 22 Fed. 197 (*semble*), *Accord*. But see *Demarest v. Flack* (1891), 128

**BUILDING & LOAN ASSOCIATION OF DAKOTA v.
CHAMBERLAIN.**

1893. 4 South Dakota 271, 56 N. W. 897.*

ACTION by the Building and Loan Assn. of Dakota against Albert E. Chamberlain et al. From a judgment overruling his demurrer to the complaint, defendant Chamberlain appeals. Affirmed.

BENNETT, P. J.—This was an action brought by the respondent in the court below upon a contract for the payment of money, executed by the defendant, Albert E. Chamberlain, and to foreclose a mortgage upon real estate, which was given by him to secure the payment of said money. * * *

The only ground, in this appeal, upon which the defendant Albert E. Chamberlain seeks to be released from the obligations created by the contract and mortgage executed by himself and wife, is that the plaintiff has no valid existence, and is therefore incapable of maintaining an action to enforce this or any other contract. In support of this contention, he insists that the acts of the territorial legislature of 1885 and 1887, under which said association was organized, were enacted without authority, and are unconstitutional and void. On this point it is sufficient to say that whatever may be the fact in relation to the valid legal existence of said association, as a corporation, the defendant Chamberlain is not in a position to challenge its validity. The complaint shows that he was a stockholder in it, and, as such, he contracted with it, borrowing and receiving money of it, and endeavored to, and did receive benefits from it, under the rules and regulations, it is presumed, he helped to make. The rule is well established that a party who has contracted with a corporation *de facto*, as such, cannot be permitted, after receiving the benefits of his contract, to allege any defects in the organization of such corporation, affecting its capacity to enforce such contract; but all such objections, if valid, are available only on behalf of the sovereign power of the state. On this proposition see 2 Mor. Corp. § 750, and authorities cited in note. This rule applies, also, where the corporation is organized under a law alleged to be unconstitutional. 2 Mor. Corp. § 759; *Freeland v. Insurance Co.*, 94 Pa. St. 504; *McCarthy v. Lavasche*, 89 Ill. 270; *Dows v. Naper*, 91 Ill. 44; *St. Louis v. Shields*, 62 Mo. 247; *Wright v. Lee*, (S. D.) 51 N. W. 706; *Wentz v. Lowe*, (Pa. Sup.) 3 Atl. 878; *Smith v. Sheeley*, 12 Wall. 358; *Irrigation Co. v. Warner*, (Cal.) 14 Pac. 37. It is true that a corporation formed in violation of a prohibition of the organic law of a territory, or the constitution of a state, like a corporation formed in violation of a prohibitory act of the legislature, will not,

N. Y. 205, 28 N. E. 645; *Lancaster v. Amsterdam Improvement Co.* (1894), 140 N. Y. 576, 35 N. E. 964; *Cochran v. Arnold* (1868), 58 Pa. St. 399. Cf. *Gow v. Collin & Co. Lumber Co.* (1896), 109 Mich. 45, 66 N. W. 676.—Eds.

* Statement abridged. Portion of opinion omitted.—Eds.

as a rule, be recognized by the courts, for the purpose of suing and enforcing rights founded on such illegal incorporation. There is, however, a difference between a constitutional prohibition designed to prevent the formation of corporations of a certain class, or for certain purposes, and a provision whose sole object is to limit the power of the legislature to pass general or special incorporation laws. An act of incorporation passed by the legislature in violation of a provision of the latter description would undoubtedly be void, and no right or authority could be derived from it; but, if persons could actually form a corporation under the provisions of such void act, they would not thereby violate the constitutional prohibition. Morawetz in his *Law of Private Corporations*, (Section 759) says: "The formation of the corporation, under these circumstances, would merely be contrary to the general common-law prohibition, as in any other case where a corporation is formed without the consent of the sovereign. The legal status of a corporation formed under an unconstitutional law, as that of a corporation formed under no law at all, or without complying with such laws as may exist, both with regard to the rights and obligations of its members, and the rights and obligations of the corporation in respect to parties dealing with it, should therefore be the same." Accordingly, it was held by the Supreme Court of Pennsylvania, in an action brought by a mutual insurance company against a policy holder, that the defendant could not, after acting as a shareholder, avoid his agreement on the ground that the corporation was incorporated under an unconstitutional law. *Freeland v. Insurance Co.*, 94 Pa. St. 504. See, also, *McClinch v. Sturgis*, 72 Me. 288.

The case of *McCarthy v. Lavasche*, 89 Ill. 270, was a suit brought by a creditor of a corporation to enforce the individual liability of a shareholder for double the amount of his shares. The defense was interposed that the act of the legislature under which the corporation was formed was unconstitutional. The Supreme Court, however, held that the defendant was liable. Justice Walker, in delivering the opinion of the court, said: "It is urged that the corporation was never legally organized, as the act under which the stockholders incorporated was unconstitutional and void; that if not, then the clause in the charter rendering stockholders liable is too vague to render them liable to the individual creditors of the company; or, if it shall be held that they are so liable, then the remedy is in equity, against all the stockholders. On the other hand it is contended that the law does not contravene the constitution; but if it should be so held, the stockholders having organized the corporation, and held themselves out to the world as such, and thereby obtained credit and incurred indebtedness, they are estopped to deny the validity of the act, or their organization under it; and that a reasonable and fair construction of the clause of the act quoted renders the shareholders individually liable to each and every creditor, and that the remedy for a recovery on the liability is complete at law. These are the questions raised and discussed on this record. Even if the law is uncon-

stitutional, can the promoters and those engaged in its operation, be heard to say that they may relieve themselves from liability, and from all their engagements, because the law under which they have acted is prohibited by the organic law? May shrewd, intelligent persons go to the general assembly and procure an act that they should know is prohibited by the fundamental law, avail themselves of its benefits, obtain the money of the uninformed and the confiding, and then be heard to say, we are not incorporated; our charter and organization are void, and we will hold your money? Or may those who promoted the enterprise, by becoming shareholders, to enable the company to organize, and to procure other people's money, be heard to interpose such a defense? The presumption is that each subscriber for stock knew at the time of subscription that the charter contained the provision rendering him liable for double the sum he subscribed; and such persons could not but have known that this provision would contribute largely to give credit to the concern, and greatly augment its business. The subscribers for shares of the stock, no doubt, expected to reap large profits and expected these profits to be greatly enhanced by this provision. It enabled them to point to it and assure individuals and the public that the institution was safe, as, if the business was not lucrative, all the stockholders were severally liable for double the amount of their subscriptions. They thus, no doubt, did increase their business, and thus obtained money and credit, which now, when the institution has proved a failure, they endeavor to avoid paying by urging that their organization, and, consequently, their subscriptions to its stock, were void. Fair dealing would say that they should be estopped from interposing such a defense. * * * Here, appellant approved of the act, availed himself of its benefits by subscribing for stock and becoming entitled to exercise all the rights and privileges of a stockholder in the corporation. Justice, morality, public policy, and precedent all demand that appellant should be estopped from denying the constitutionality of the law.

If stockholders might show the law unconstitutional, and their organization void, and all their acts unauthorized, then all persons engaged in the organization of the corporation should be held liable for the consequences of their illegal and unauthorized acts, independent of the clause in their charter. So they should, in no event, escape liability for obtaining money without authority."

The rule in Michigan appears to be different, and, when a corporation is organized under a void act of the legislature, the courts will not recognize the corporation for the purpose of enforcing a contract made by or with it. The cases which have been decided by the Supreme Court of that state in which the question arose viz.: *State v. How*, 1 Mich. 512; *Green v. Graves*, 1 Doug. (Mich.) 351; *Hurlbut v. Brittain*, 2 Doug. (Mich.) 191; *Burton v. Schilbach*, 45 Mich. 504, 8 N. W. 497; *Mok v. Association*, 30 Mich. 511,—were cases where the corporations appeared to have been formed for illegal purposes, namely, to violate laws against unauthorized bank-

ing, as well as without constitutional legislative authority. But that court seems to have receded somewhat from this position in the later case of *Manufacturing Co. v. Runnells*, (Mich.) reported in 20 N. W. 823. This was an action to recover the possession of certain real estate. Upon the trial of the case, the plaintiff offered in evidence a sheriff's certificate of sale of the real estate, made by virtue of an execution issued upon a judgment rendered in favor of the plaintiff corporation. To the introduction of this, the defendant objected for the reason that the grantee named in the certificate is a corporation, and cannot hold real estate by its articles of corporation, or under the laws of that state. The Circuit Court trying the case overruled the objection. Upon appeal the Supreme Court says: "In this case the defendant introduced in evidence the execution upon which the sale was made. From this appears that it was issued upon a judgment rendered for damages for the nonperformance of certain promises and undertakings made by the defendant to the Estey Manufacturing Company, which shows that the defendant had had dealings with the plaintiff as a corporation, in the name it assumed. It was therefore estopped, not only by having dealt with it as a corporation, but by the judgment in the case, to deny its corporate existence."

So far as this question arises in our jurisdiction, it is well settled by Section 2892 of the Compiled Laws, which is as follows: "The due incorporation of any company, claiming in good faith to be a corporation under this chapter and doing business as such, or its right to exercise corporate powers shall not be inquired into collaterally, in any private suit to which such de facto corporation may be a party; but such inquiry may be had and action brought, at the suit of the territory, in the manner described in the Code of Civil Procedure."

This seems, therefore, to be the well-established doctrine throughout American jurisprudence. Any other doctrine would be contrary to the plainest principles of reason and good faith, and involves a mockery of justice. Parties must take the consequences of the position they assume. They are estopped to deny the reality of the state of things which they have helped to make appear to exist, and upon which others have relied. Therefore, we are of the opinion that the court below committed no error in overruling the demurrer upon this ground, and the order of the court below is *affirmed*. All the judges concur.⁷

⁷ *Agua Fria Copper Co. v. Bashford & Co.* (1894), 4 Ariz. 203, 35 Pac. 983; *Planters' & Miners' Bank v. Padgett* (1882), 69 Ga. 159; *McCarthy v. Lavasche* (1878), 89 Ill. 270; *Winget v. Quincy Building & Assn.* (1889), 128 Ill. 67, 21 N. E. 112; *Briggs v. Cape Cod Canal Co.* (1884), 137 Mass. 71 (expired law); *Gardner v. Minneapolis & C. R. Co.* (1898), 73 Minn. 517, 76 N. W. 282; *Coxe v. State* (1895), 144 N. Y. 396, 39 N. E. 400; *Commonwealth v. Phila. County* (1899), 193 Pa. St. 236, 44 Atl. 336; *Miller v. Coal Co.* (1888), 31 W. Va. 836, 8 S. E. 600 (expired law); *Close v. Glenwood Cemetery* (1882), 107 U. S. 466, 27 L. ed. 408, 2 Sup. Ct. 267, *Accord*. See *contra*, *Brandenstein v. Felsa* (1894), 101 Cal. 336 (unconstitutional law); *Eaton v.*

CLARK v. AMERICAN CANNEL COAL CO.

1905. 165 Ind. 213, 73 N. E. 1083.

SUIT by the American Cannel Coal Co. against Emma L. Clark. From a decree for plaintiff, defendant appeals. Reversed.

MONKS, J.—This suit was brought by appellee to enjoin appellant from mining and removing fire-clay from certain real estate in Perry county, and to quiet appellee's title to said fire-clay. Appellee sold and conveyed said real estate by deed to a remote grantor of appellant on September 20, 1866, and claims to own said fire-clay by virtue of the reservation contained in said deed. A trial of said cause resulted in a final decree quieting appellee's title to said fire-clay and enjoining appellant from removing the same.

The first question to be determined is: was appellee, when it commenced this suit, an existing corporation having the power to sue? If this question be answered in the negative this case must be reversed. It appears from the record that appellee—a corporation—was created by special act (Local Laws 1838, p. 216), to continue for a period of fifty years from December 23, 1837. The powers granted were to mine for coal, "purchase, receive, hold and enjoy lands, coal, iron and other mines, * * * and the same to sell, convey and demise." In 1885 the legislature passed an act (Acts 1885, p. 121, §§ 5124-5128, Burns 1901), which purported to extend the corporate existence of every private corporation, created or organized by special act for the purposes of mining stone, coal, iron ore, etc., thirty years after the passage of said act, whose board of directors, within sixty days after the passage of said act of 1885, shall avail itself of the provisions of said act by adopting resolutions to that effect, and filing the same with a statement giving the title and date of the act creating said corporation and of each act amendatory or supplemental to said creative act. The board of directors of appellee complied with the requirements of said act of 1885 on May 30, 1885, and appellee claims that thereby its corporate existence was extended thirty years from that time. Since 1837 until the commencement of this action appellee has exercised corporate powers under said special act of 1837 and the act of 1885. Appellant's position is that, as the special act of December 23, 1837, creating appellee a corporation, fixed the life of said corporation at fifty years, it ceased to exist when that period was ended, in 1887; that said act of 1885 was unconstitutional, and the attempt to continue the corporate existence of appellee by complying with its provisions was

Walker (1889), 76 Mich. 579, 43 N. W. 638 (same); Bradley v. Reppell (1895), 133 Mo. 545, 32 S. W. 645, 34 S. W. 841 (expired law); Sturges v. Vanderbilt (1878), 73 N. Y. 384 (same); Davis v. Stevens (1900), 104 Fed. 235 (no law).

See also Jennings v. Dark (Ind., 1910), 92 N. E. 778, and note, 11 Columbia Law Rev. 160; Brady v. Delaware Ins. Co. (1899), 2 Penn. (Del.) 237, 45 Atl. 345, and note, 13 Harvard Law Rev. 690.—Eds.

without effect; that appellee having ceased to exist as a corporation, cannot maintain this action. The act of April 2, 1885, *supra*, which appellee claims continued its corporate existence for thirty years from the date of its passage, is clearly unconstitutional under the rule declared in *In re Bank of Commerce* (1889), 153 Ind. 460, 47 L. R. A. 489.

Appellee insists, however, that appellant cannot raise any question in regard to the constitutionality of said act of 1885 in this case, because (1) it is at least a *de facto* corporation, and therefore impervious to collateral attack; (2) that appellant is estopped from denying its corporate existence. It is true, as claimed by appellee, that the corporate existence of a *de facto* corporation can only be questioned in a direct proceeding brought for that purpose. *Doty v. Patterson* (1900), 155 Ind. 60, 64, and authorities cited. It is essential to the existence of a *de facto* corporation, however, that there be (1) a valid law under which a corporation with the powers assumed might be incorporated; (2) a bona fide attempt to organize a corporation under such law; (3) and an actual exercise of corporate powers. *Doty v. Patterson*, *supra*; 10 Cyc. Law & Proc., 252-256; 1 Clark & Marshall, Priv. Corp., §§ 82a, 82b. It follows, therefore, that there cannot be a corporation *de facto* when there cannot be one *de jure*. If there is no law under which a corporation *de jure* might exist, its nonexistence may be set up even in a collateral proceeding, 10 Cyc. Law & Proc., 255, 256; 1 Clark & Marshall, Priv. Corp., § 82c; *Heaston v. Cincinnati, etc., R. Co.* (1861), 16 Ind. 275, 279, 79 Am. Dec. 430; *Harriman v. Southam* (1861), 16 Ind. 190; *Snyder v. Studebaker* (1862), 19 Ind. 462, 81 Am. Dec. 415; *Eaton v. Walker* (1889), 76 Mich. 579, 43 N. W. 638, 6 L. R. A. 102; *Georgia, etc., R. Co. v. Mercantile Trust, etc., Co.* (1894), 94 Ga. 306, 21 S. E. 701, 32 L. R. A. 208, 47 Am. St. 153. "To be a corporation *de facto* it must be possible to be a corporation *de jure*, and acts done in the former case must be legally authorized to be done in the latter, or they are not protected or sanctioned by the law. Such acts must have an apparent right," *Evenson v. Ellingson* (1887), 67 Wis. 634, 646, 31 N. W. 342. It necessarily follows that there cannot be a corporation *de facto* under an unconstitutional statute, for such a statute is void, and a void law is no law. 1 Clark & Marshall, Priv. Corp., p. 246; *Black, Const. Law*, p. 64; *Snyder v. Studebaker*, *supra*; *Harriman v. Southam*, *supra*; *Heaston v. Cincinnati, etc., R. Co.*, *supra*; *Eaton v. Walker*, *supra*; *Norton v. Shelby County* (1886), 118 U. S. 425, 6 Sup. Ct. 1121, 3 L. ed. 178.

If the law under which a corporation is organized, or the special act creating the corporation, fixes a definite time when its corporate life must end, it is evident that when that date is reached, said corporation is *ipso facto* dissolved without any direct action on the part of the state or its members. And no corporate powers can thereafter be exercised by it except such as are given it by statute for the purpose of winding up its affairs, which in this State is limited to three years after the dissolution. § 3429 Burns 1901, § 3006 R. S. 1881,

and Horner 1901; 10 Cyc. Law & Proc., 1271; 2 Clark & Marshall, Priv. Corp., § 305; 2 Morawetz, Priv. Corp. (2d ed.), § 1031; 2 Beach, Priv. Corp., § 780; People, ex rel., v. Anderson, etc., R. Co. (1888), 76 Cal. 190; Scanlan v. Cranshaw (1878), 5 Mo. App. 337; La Grange, etc., R. Co. v. Rainey (1870), 47 Tenn. 420, 432; Grand Rapids Bridge Co. v. Prange (1887), 35 Mich. 400, 24 Am. Rep. 585; Bradley v. Reppell (1896), 133 Mo. 545, 32 S. W. 645, 34 S. W. 841, 54 Am. St. 685; May v. State Bank (1843), 2 Rob. (Va.) 56, 40 Am. Dec. 726; Rider v. Nelson, etc., Factory (1836), 7 Leigh (Va.) 156, 30 Am. Dec. 495.

Appellee in 1866 at the time its deed for the land in controversy was executed to appellant's remote grantor, was a corporation de jure by virtue of the special law of December 23, 1837 (Local Laws 1838, p. 216). Even if appellant who claims the real estate in controversy and the right to mine said fire-clay and remove the same under appellee's deed of September 20, 1866, is estopped to deny its corporate existence, such estoppel only operates to prevent a denial of its corporate existence at the time the deed was executed in 1866, and in no way prevents appellant from alleging facts showing that the period fixed for its existence as a corporation expired in 1887, and that there was no such corporation in existence when this action was commenced. This is true because after a corporation is dissolved by a judicial decree or by the expiration of the period fixed for its existence in the law under which it is organized, it is not even a de facto corporation, and its existence as a corporation may be questioned collaterally. 1 Clark & Marshall, Priv. Corp., 247; 2 Clark & Marshall, Priv. Corp., § 305; Guaga Iron Co. v. Dawson (1836), 4 Blackf. 202; Morgan v. Lawrenceburgh Ins. Co. (1852), 3 Ind. 285; Brookville, etc., Turnpike Co. v. McCarty (1856), 8 Ind. 392, 65 Am. Dec. 768; Bradley v. Reppell, supra; Krutz v. Paola Town Co. (1878), 20 Kan. 397; Marysville Investment Co. v. Munson (1890), 44 Kan. 491, 24 Pac. 977; Supreme Lodge Knights of Pythias v. Weller (1896), 93 Va. 605, 25 S. E. 891; Dobson v. Simonton (1882), 86 N. C. 492; Asheville Division, etc., v. Aston (1885), 92 N. C. 578; Sturges v. Vanderbilt (1878), 73 N. Y. 384; White v. Campbell (1844), 5 Humph. (Tenn.) 37.

As the corporate existence of appellee fixed by the special act of 1837 ended in 1887, and the three years given by § 3429, Burns 1901, § 3006 R. S. 1881 and Horner 1901, for the purpose of winding up its affairs ended in 1890, and the act of 1885 (Acts 1885, p. 121), under which appellee claims its corporate existence was extended thirty years, is unconstitutional, it follows that appellee had no power to sue when this action was commenced.

Judgment reversed, with instructions to sustain appellant's motion for a new trial of the issues joined on the answers in abatement, and for further proceedings in accordance with this opinion.

CINCINNATI, ETC., R. CO. v. DANVILLE, ETC., R. CO.

1874. 75 Ill. 113.

APPEAL from the Circuit Court of Iroquois county; the Hon. Charles H. Wood, Judge, presiding.

This was a bill for an injunction, filed by the appellant against the appellee, to restrain the latter taking possession of the railroad and right of way of the complainant under certain fraudulent proceedings for the condemnation of the same.

MR. JUSTICE MCALLISTER delivered the opinion of the court:

In the year 1871, certain persons, purporting to be twenty-five in number, proceeded to organize themselves, under the general railroad law of 1849, into the appellant corporation, for the purpose of supplying a portion in this state of what was necessary to constitute a complete line of railway between the cities of Cincinnati, Ohio, and Chicago, in this state. The amount of stock was fixed, was subscribed, and paid; directors were elected, articles of association prepared, subscribed, certified and filed with the Secretary of State, and the usual certificate given by that officer.

The portion of the line to be constructed was from a point on the line between this state and Indiana, about three miles southeast of Sheldon, in Iroquois county, thence running northeasterly through that county and a portion of Kankakee county to the village of St. Anne.

Appellant did not assume to exercise the right of eminent domain, but obtained the right of way, so far as it was obtained, by purchase or contract. It located its road between the points stated, and, by about the middle of December, 1871, had it constructed, so that about the 1st of May, 1872, the through line, including the portion in question, was opened for public use as a railroad, and appellant has not only been in the exercise of its functions and franchises as a railroad corporation, but the same has been open, public, and notorious. In November, 1872, this company re-organized under the general railroad act of this State, which went into force March 1, 1872.

It appears also that about the 13th of November, 1872, the appellee was organized under the last-mentioned act, as a railroad corporation, to construct a road, in part at least, upon a route similar to that of appellant. On the 22d of November, 1872, appellee, having caused a survey of its line and a plat to be made, presented a petition to the county court of Iroquois county for the purpose, ostensibly, of condemning land through that county for its right of way. Numerous tracts and parcels are described and the names of owners or pretended owners given. Appellant is not named or described in the petition. Nor was any notice to appellant given or contemplated. Such proceedings were had upon this petition, that a jury was summoned to ascertain the compensation. About this time, appellant discovered that although it was in the actual possession and use of

the right of way, before mentioned, as a common carrier, and this fact must have been known to the agents and attorneys of appellee, yet the land which appellee was about to have condemned was, in fact, the very right of way of which appellant was in the actual and open possession for public purposes, and to this circumstance there was not the remotest allusion in appellee's petition. It appearing that there was no necessity or even plausible excuse for thus interfering with appellant's right of way, then, in view of the circumstance of appellant's open and notorious possession of it, and the studious exclusion of all these facts from appellee's petition, and the failure to make appellant a party, with notice, the inference is irresistible, that this proceeding in the county court was designed for the fraudulent purpose of surreptitiously gaining possession of appellant's right of way. The actors in the formation of the scheme, as would seem from their positions in argument on this appeal, reasoned in this wise: "Now, there are defects in the organization of the Cincinnati, LaFayette & Chicago Railroad Company; they have made a slip in some particulars, and if we can so manage as to get a condemnation proceeding through the court without notice to that company, and thereby get into possession, we can then assail their organization, convince the court that they can have no standing in court on account of those defects, and thus keep that possession, no matter how acquired." That is the very argument they urge here to sustain the decree of the court below dismissing appellant's bill to restrain them from thus obtaining possession, on the ground of fraud and want of jurisdiction in the proceedings to condemn. It is apparent from the face of those proceedings, when considered with the surrounding circumstances, that the former, though ostensibly for the ordinary purpose of condemning land not appropriated to railroad uses, for appellee's right of way, were, in reality, but in the execution of a scheme devised for the fraudulent and inequitable purpose of getting possession of appellant's right of way without making compensation, and then, to seize upon alleged defects in appellant's organization, as a means of retaining it against justice and right. The morality of the act is supported by the same reasoning which would be resorted to in justification of a contemplated theft from one non compos mentis, "He is incapable of appearing in court to vindicate his rights."

An elaborate printed argument has been presented by appellee's counsel to show that appellant was not rightfully organized, and that therefore it could acquire no right of way, and especially that it can have no standing in court in its claim for protection against this contemplated invasion of its possession. He says the act of 1849 was repealed by the constitution of 1870.

There is, in our opinion, no basis for the position that the sections of the act of 1849, so far as they provide for the formation of such corporations, are abrogated by the constitution. They are not inconsistent with any of its provisions. Then, there being such a law authorizing the formation of railroad corporations, and articles of

association having been prepared and filed with the secretary of state, and he having given the certificate provided for, and there having been a user of the franchises purporting to be invested in the association, the latter became a de facto corporation, and under the settled law of this court neither the eligibility of the directors nor the rightfulness of the existence of the corporation could be inquired into collaterally in this suit. *Tarbell v. Page*, 24 Ill. 46; *Mitchell et al. v. Deeds*, 49 ib. 416; *Thompson v. Candor*, 60 ib. 244.

In *Mitchell v. Deeds*, before cited, the court, page 422, said: "The law is well settled in this State, that, under the plea of nul tiel corporation, the plaintiff need only show an organization in fact and a user of corporate franchises."

So, by parity of reasoning, such organization in fact, and user, are all that is necessary to maintain a bill in equity against a mere stranger seeking to interfere with the property of such de facto corporation. Here, it was indisputably shown that there was such an organization in fact, followed by user of corporate franchises. That was sufficient. So, also, was it shown that the directors were elected under color of authority and were acting as such. They were, therefore, de facto officers of the corporation. Their title to the office could not be brought in question and decided collaterally in this suit. *Lawson et al. v. Kolbenson et al.*, 61 Ill. 418, and authorities there cited.

Appellee had authority to exercise the right of eminent domain, but, by the statute prescribing the mode of its exercise, it could not have appellant's right of way condemned for even a qualified or conjoint use, without describing it in the petition as such right of way, and alleging inability to agree as to compensation. This proceeding, which might perhaps have been lawful and proper but for circumstances which were studiously concealed, was for an inequitable purpose. It was designed and carried forward for the purpose of getting possession of a right of way of which appellant was in the quiet possession as owner, without making appellant a party or paying to it any compensation. No other object was intended by, and no other result could follow, the carrying the proceeding through to a finality. It was, in this view, a proper case for an injunction. In *Goodenough v. Sheppard*, 28 Ill. 81, it was held that a person in the quiet possession of real estate as owner may obtain an injunction to restrain others from dispossessing him by means of process growing out of litigation to which he was not a party. It does not lie with appellee to say, in justification of this unequitable proceeding, that appellant was not so far rightfully organized or authorized to construct the railroad in question as to be capable of holding lands for the purposes of a right of way. That is a question solely between appellant and the persons from whom title was obtained, or between appellant and the people of the state, when proper proceedings shall arise to require its decision.

It is obvious, from the record, that the court below made inquiry into the rightfulness of appellant's corporate existence, and dis-

missed the bill for defects in its organization. This was error. The decree will be reversed, and cause remanded for further proceedings not inconsistent with this opinion.

*Decree reversed.*⁸

BUTCHERS' & DROVERS' BANK OF ST. LOUIS v.
McDONALD.

1881. 130 Mass. 264.⁹

CONTRACT upon a promissory note signed by defendant's testator. The issue raised was as to the legality of plaintiff's organization.

BY THE COURT.—The plaintiff being a corporation *de facto*, and the defendant having contracted with it as such, the legality of its organization cannot be impeached by him when sued upon his contract.

*Exceptions overruled.*¹⁰

CENTRAL OF GEORGIA RY. CO. v. UNION, ETC., RY. CO.

1905. 144 Ala. 639, 39 So. 473.¹¹

APPEAL from Bullock Circuit Court. Appellee filed in the probate court of Bullock county an application to condemn certain lots in the town of Union Springs belonging to appellant. There was

⁸ "But for the purpose of enforcing a contract, made with a supposed corporation as such, or of protecting the property of such a corporation from tortfeasors, it is enough to show a corporation *de facto*." Phelps, J., in *Searsburgh Turnpike Co. v. Cutler* (1834), 6 Vt. 315, at page 323. And so, *Stockton &c. Road Co. v. Stockton &c. Railroad Co.* (1873), 45 Cal. 680; *Elizabeth City Academy v. Lindsey* (1846), 6 Ired. Law (28 N. C.) 476; *Remington Paper Co. v. O'Dougherty* (1875), 65 N. Y. 570; *Baltimore &c. R. Co. v. Fifth Baptist Church* (1890), 137 U. S. 568, 34 L. ed. 784, 11 Sup. Ct. 185.

As to liability of stockholders of a *de facto* corporation in tort, see *Vredenburg v. Behan* (1881), 33 La. Ann. 627; *Lamming v. Galusha* (1894), 81 Hun (N. Y.) 247, 30 N. Y. S. 767, *affd.* 151 N. Y. 648, 45 N. E. 1132; *Pinkerton v. Pennsylvania Traction Co.* (1899), 193 Pa. St. 229, 44 Atl. 284; *Miller v. Coal Co.* (1888), 31 W. Va. 836, 8 S. E. 600.—Eds.

⁹ Statement rewritten.—Eds.

¹⁰ "So far as defendant's claim that plaintiff is not legally incorporated is concerned, assuming such to be the fact, it may be observed that the general rule is that persons sued by a corporation in an action *ex contractu*, as well as persons sued by a corporation in an action *ex delicto*, are equally debarred from setting up the defense that the corporation was not legally organized, which is a question for the State." *National Society v. American Surety Co.* (1907), 56 Misc. (N. Y.) 627, 107 N. Y. S. 820.

As to the right of a defectively incorporated association, which is not a *de facto* corporation, to sue either in contract or in tort, see articles by E. H. Warren, "Collateral Attack on Incorporation," in 20 *Harvard Law Rev.* 456, 21 *ibid.*, 305, 329-330; Machen on Corporations, § 282.—Eds.

¹¹ Statement abridged. Portion of opinion omitted.—Eds.

judgment of condemnation from which appeal was taken. Affirmed.

SIMPSON, J.—This is a proceeding by appellee to condemn a right of way over certain lots in Union Springs, Alabama.

The first proposition insisted upon by the appellant is that the appellee corporation was not duly organized according to our statutes, and consequently, had no right to condemn the right of way. It claims that the corporation was not duly organized because the certificate of its organization does not contain the names of the incorporators. While it is true that 1163 of the Code does state that "when duly organized a corporation has power," etc., yet, to give that expression the strict construction contended for by the appellant, would be to declare that all other powers of the corporation are dependent upon a literal compliance with all the requirements of the statute and to abrogate the doctrine of de facto corporations and to admit the plea of nul tiel corporations in all suits brought by them.

It is true that in 2nd Cook on Corporation, (5th ed.), § 637, it is stated that "where a railroad corporation attempts to acquire a right of way, the person, whose property will be affected thereby, may oppose the acquisition of the right of way by showing that the company is not legally incorporated," but a reference to the case on which that remark is based shows that the act under which the corporation professed to act required it to begin construction and expend ten per cent. of its capital within five years, and specially declared that if it did not do so "its corporate existence and powers should cease." Nothing had been done and there was no pretense of a de facto corporation.—*Brooklyn W. & N. Ry. Co. v. Broadway Ry. Co.*, 72 N. Y. 245.

In the same section the learned author goes on to state that, "If there is a law authorizing incorporation, and a company has attempted to organize under it, and has acted as a corporation it is a de facto corporation, and its de jure existence can be questioned only by the state." This proposition is fully borne out by the great weight of authority, notwithstanding the remarks contra in the cases of *N. Y. Cable Co. v. Mayor*, 104 N. Y. 43; *Independent Order, etc., v. United Order of Foresters*, 94 Wis. 234, 239-40; *Brown v. Calumet River Ry.*, 125 Ill. 600, 606; *Portland & Greenwood Turnpike Co. v. Bobb*, 88 Ky. 226, 228; *Wellington & P. R. R. v. The Cashie, etc., Lumber Co.*, 114 N. C. 690.

This court has declared that "a corporation de facto exists when, from irregularity or defect in the organization or constitution, or from some omission to comply with the conditions precedent, a corporation de jure is not created, but there has been a colorable compliance with the requirements of some law under which an association might be lawfully incorporated for the purposes and powers assumed, and the user of the rights claimed to be conferred by the law—when there is an organization with color of law and the exercise of corporate franchises," and it also states that such de facto corporations "are under the protection of the same law and governed

by the same legal principles as those of the former so long as the state acquiesces in their existence and the exercise of corporate functions. A private citizen, whose rights are not invaded, who has no cause of complaint has no right to inquire collaterally into the legality of its existence. This can only be done by a direct proceeding on the part of the state, from whom is derived the right to exist as a corporation whose authority is usurped."—*Owensboro Wagon Co. v. Bliss*, 132 Ala. 253, 256. See also *Bibb v. Hall*, 101 Ala. 80, 96.

It is not necessary to decide whether or not the facts show a substantial compliance with the statute. * * *

We find no error in the record and the judgment of the court is affirmed.

HARALSON, DOWDELL and DENSON, JJ., concurring.¹²

SOCIETY PERUN v. CLEVELAND.

1885. 43 Ohio St. 481, 3 N. E. 357.

ERROR to the District Court of Cuyahoga county.

On the 28th of January, 1874, the city of Cleveland conveyed to Perun (an incorporated school and library society), certain real estate situated in that city, and to secure the unpaid purchase-money therefor, Perun, on the same date, executed and delivered to the city

¹² *Spring Valley Water Works v. San Francisco* (1863), 22 Cal. 434; *McAuley v. Columbus &c. R. Co.* (1876), 83 Ill. 348; *Ward v. Minnesota &c. R. Co.* (1887), 119 Ill. 287, 10 N. E. 365; *Morrison v. Indianapolis &c. R. Co.* (1905), 166 Ind. 511, 76 N. E. 961, 77 N. E. 744 (valuable list of authorities); *Detroit &c. R. Co. v. Campbell* (1905), 140 Mich. 384, 103 N. W. 856; *Wellington &c. R. Co. v. Cashie &c. Lumber Co.* (1894), 114 N. C. 690, 19 S. E. 646; *Oregon Short Line R. Co. v. Postal Tel. Cable Co.* (1901), 111 Fed. 842, 49 C. C. A. 663; *Postal Tel. Cable Co. v. Oregon Short Line R. Co.* (1902), 114 Fed. 787, *Accord*.

The power of exercising eminent domain is denied to a *de facto* corporation in the following cases. *Williamson v. Kokomo &c. Fund Assn.* (1883), 89 Ind. 389 (*semble*); *St. Joseph R. Co. v. Shambaugh* (1891), 106 Mo. 557, 17 S. W. 581; *New York Cable Co. v. Mayor &c. of New York* (1887), 104 N. Y. 1, 10 N. E. 332; *Atlantic R. Co. v. Sullivan* (1855), 5 Ohio St. 276; *Atkinson v. Marietta R. Co.* (1864), 15 Ohio St. 21; *Tulare Irrigation District v. Shepard* (1901), 185 U. S. 1, 46 L. ed. 773, 22 Sup. Ct. 531. See article by C. E. Carpenter, "De Facto Corporations," in 25 Harv. Law Rev. 623, esp. p. 639.

"In order to sustain proceedings by which a body claims to be a corporation, and as such empowered to exercise the right of eminent domain, and under that right to take the property of a citizen, it is not sufficient that it be a corporation *de facto*. It must be a corporation *de jure*. Where it is sought to take the property of an individual under powers granted by an act of the legislature to a corporation to be formed in a particular manner therein directed, the constitutional protection of the rights of private property requires that the powers granted by the legislature be strictly pursued, and all the prescribed conditions be performed." *Rapallo, J., in New York Cable Co. v. Mayor &c., of New York* (1887), 104 N. Y. 1, at page 43, 10 N. E. 332.—Eds.

its four promissory notes and a mortgage upon the premises conveyed.

The city neglected to file this mortgage for record until the 21st day of October, 1879. In February, 1874, certain persons attempted to organize a mutual benefit association under an act supplementary to an act to provide for the creation and regulation of incorporate companies passed May 1, 1852 (S. & C. Stat. 271), passed April 20, 1872 (69 Ohio L. 82), under the corporate name of Society Perun. Thereafter, in May, 1874, Perun delivered to Society Perun its deed purporting to convey to the latter the premises theretofore mortgaged to the city. From that time forward, and prior to the filing of the city's mortgage for record, Society Perun, acting in its supposed corporate capacity, from time to time, executed and delivered deeds, mortgages, and executory contracts of sale, purporting to convey, incumber and sell parcels of these mortgaged premises to various parties, who were made defendants in the action below, and some of whom (including Amasa Stone, a mortgagee, and who had paid taxes upon the premises mortgaged to him), are cross-petitioners in error. Thereafter, in June, 1880, in a proceeding in *quo warranto*, in this court, instituted by the Attorney-General, Society Perun was adjudged not to have become incorporated in conformity to the laws of this state, but that its pretended incorporation was in violation thereof; and it was accordingly ousted of all rights and franchises to be a corporation.

These proceedings in *quo warranto* were had pending, and prior to the final judgment in the action below, which was brought by the city to foreclose her mortgage, and also to foreclose her supposed vendor's lien on the mortgaged premises, as against these subsequent grantees, mortgagees, and purchasers.

The cause was appealed from the court of common pleas to the district court, wherein it was tried upon the issues, the court finding among other things, that, as to the city of Cleveland, Society Perun was not a corporation either in law or in fact, and that the conveyance to it by Perun was void as against the city; and that the mortgages and other liens and claims of all the defendants (except the lien of Amasa Stone for taxes, and the claims of certain defendants for improvements on the premises), were subsequent and inferior to the lien of the city, in whose favor the court adjudged the second lien, and subsequent only to the lien of Amasa Stone for taxes paid by him, but of equal rank and merit with the holders of liens for expenditures on account of improvements above mentioned.

By the judgment in the *quo warranto* proceeding it was by this court in form adjudged that the defendants (the pretended incorporators) ever since their pretended incorporation, had unlawfully and without authority exercised the franchises of, and usurped the right to be, a body corporate; that the pretended organization of these defendants as a corporation was wholly void and of no effect, and

vested in them no corporate rights, powers, privileges, or franchises of any description whatever.

It was further in form adjudged that the defendants never had, nor had any of them, the authority or lawful right to be a body corporate or to exercise or hold any of the powers, rights and liberties, privileges, functions or franchises of a body corporate; but that they and each of them in the use and exercise of the same were and had ever been usurpers thereof. The sole ground upon which this judgment of ouster was rendered was that while the statute required that they should set forth in their certificate of incorporation (among other things) the manner of carrying on the business of the association, the attempted compliance with this requirement was in these words:

"Third. That the manner of carrying on business of said association shall be such as may be from time to time prescribed by the by-laws of such association; provided that the same shall not be inconsistent with the laws of the state of Ohio."

Upon the trial below the plaintiff gave in evidence, against the objection of defendants, the record of the quo warranto proceedings.

The defendants offered in evidence the writing which was filed with the secretary of state as the certificate of incorporation of Society Perun.

They also offered to prove that the pretended incorporators proceeded to comply strictly with the requirements of the statutes; that they elected trustees, prepared a certificate of incorporation stating explicitly the manner of carrying on the business; that this was forwarded to the secretary of the state, who submitted it to the attorney-general for examination and approval; that the secretary of state returned this paper with another form of certificate which had been approved by the attorney-general and secretary of state, and which was the identical certificate actually filed with the secretary of state, and under the supposed authority of which an organization was in good faith attempted, and that they proceeded in good faith to act and transact its business under the supposed authority of such incorporation.

All this was excluded, and the defendants excepted. To reverse this judgment the present proceeding is prosecuted.

The alleged errors chiefly relied upon are the exclusion of the evidence offered to prove an attempt, in good faith, to incorporate Society Perun; the finding and holding of the court that Society Perun had never been in law or fact a corporation; that as against the city the deed from Perun was void; and adjudging the city's lien to be prior to the rights and liens of Society Perun and its mortgagees, grantees and purchasers.

OWEN, J.—The defendants below, conceding that Society Perun had never been a corporation *de jure*, maintain that the court below should have permitted them to prove that such society was a *de facto* corporation; that it attempted, in good faith, to become a body corporate; proceeded to act and transact business in good faith under

the supposed authority of incorporation, and that its acts ought not to have been declared to be wholly void as against the city of Cleveland.

The judgment of ouster was an adjudication between the state and the society upon the right of the latter to exercise corporate franchises. For the purposes of such adjudication it was competent for this court to consider and determine what had been its *status* from its first attempt to incorporate. (But it had no power to pass upon or determine the rights of parties not before it)

It was not competent for this court to determine in that proceeding that Society Perun had never been a corporation *de facto*, or that its acts and business transactions, under the color of its supposed charter powers, were void. The authority of the court in that behalf was derived from sec. 6774 (Rev. Stats.), which provides: "When a defendant is found guilty of usurping, intruding into, or unlawfully holding or exercising an office, franchise, or privilege, judgment shall be rendered that such defendant be ousted and altogether excluded therefrom, and that the relator recover his costs."

When the court had excluded the society from its franchises to be a corporation, it exhausted its jurisdiction over the subject-matter. It had no power to speak concerning whatever rights may have been acquired by the society as a corporation *de facto*, or by third parties in their transactions with it as an acting corporation.

It is conceded by the city that parties who had recognized the existence of the society by their transactions with it as a supposed corporation are estopped to deny its corporate existence. But it is maintained that the city, having engaged in no transactions with it, is free to challenge its existence as a corporation *de facto* as well as *de jure*. The argument is that: "No case can be found where it is held that there is a corporation *de facto* against persons who have in no way recognized its existence as a corporation," and that: "The notion of a *de facto* corporation is based on the doctrine of estoppel; when estoppel cannot be invoked there can be no *de facto* corporation."

The theory that a *de facto* corporation has no real existence, that it is a mere phantom, to be invoked only by that rule of estoppel which forbids a party who has dealt with a pretended corporation to deny its corporate existence, has no foundation, either in reason or authority. A *de facto* corporation is a reality. It has an actual and substantial legal existence. It is, as the term implies, a *corporation*.

"It is a self-evident proposition that a contract cannot be made with a corporation unless the corporation be in existence at the time. A real contract with an imaginary corporation is as impossible, in the nature of things, as a real contract with an imaginary person. It is essential, therefore, in order to establish the existence of a contract with a corporation, to show that the corporation was in existence, at least *de facto*, at the time the contract was made." Morawetz Private Corporations, § 137.

It is bound by all such acts as it might rightfully perform as a cor-

poration *de jure*. Where it has attempted in good faith to assume corporate powers; where its proceedings in that behalf are colorable, and are approved by those officers of the state who are authorized to act in that regard; where it has honestly proceeded for a number of years, without interference from the state, to transact business as a corporation; has been reputed and dealt with as a duly incorporated body, and valuable rights and interests have been acquired and transferred by it, no substantial reason is suggested why its corporate existence, in a suit involving such transactions, should be subject to attack by any other party than the state, and then only when it is called upon in a direct proceeding for that purpose, to show by what authority it assumes to be a corporation.

Proof was offered upon the trial below to show, (1) that the persons seeking to incorporate first filed with the secretary of state a certificate which fully complied with the requirements of the statutes, and free from the defect which finally proved fatal to its existence, but which was disapproved by the attorney-general; (2) That the certificate of incorporation which was finally filed with the secretary of state recited that, "said association has been formed and organized for the mutual protection and relief of its members, and for the payment of stipulated sums of money to the families or heirs of the deceased members of said association; that the officers of said association have been duly chosen; that for the purpose of becoming a body corporate under an act passed by the general assembly of the state of Ohio, entitled, an act supplementary to an act, entitled an act to provide for the creation and regulation of incorporated companies in the state of Ohio, passed May 1, 1852, passed April 20, 1872;" (3) That this certificate was approved by the secretary of state, and also by the attorney-general, as provided by the statutes (69 Ohio L. 150); (4) That it proceeded in good faith to transact business peculiar to corporations provided for by the act under which it attempted to incorporate.

All this was excluded, and the decision of the court below practically rested on the proof offered by the city, that Society Perun had been ousted of its franchises, which was evidently construed as determining that such society had from the first no corporate existence, either *de jure* or *de facto*, and consequently no capacity to receive or impart any interest in or title to real estate except as against such parties as were by reason of their recognition of or dealings with it, estopped to deny its incorporate existence.

Did the court err? This fairly presents the controlling and very important question: Was it competent to show, as against a party who was not estopped to deny its corporate existence, that Society Perun was, at the time of the transactions involved in controversy, a corporation *de facto*?

In Attorney-General ex rel. Pettee v. Stevens, Saxton (N. J. Eq.) 369, the relator sought to enjoin the Camden and Amboy R. R. and Transportation Co. and others acting under its authority from erecting a bridge over a navigable stream. The claim was that the act

authorizing the corporation had been perverted and disregarded, and that there was no legal incorporation. The relators were in no manner estopped to attack the corporate existence of the respondent. The court held:

"Where a set of men claiming to be a legally incorporated company under an act of the legislature, have done everything necessary to constitute them a corporation, colorably at least, if not legally, and are exercising all the powers and functions of a corporation; they are a corporation, *de facto*, if not *de jure*; and this court will not interfere, in an incidental way, to declare all their proceedings void, and treat them as a body having no rights or powers."

The chancellor, speaking for the court, said:

"Here, then, is a set of men claiming to be a legally incorporated company under the act of the legislature, exercising all the powers and functions of a corporation. They are a corporation *de facto*, if not *de jure*. Everything necessary to constitute them a corporation has been done, colorably at least, if not legally; and I do not feel at liberty, in this incidental way, to declare all their proceedings void, and treat them as a body having no rights or powers. It has been seen that the court will not do this where a corporation properly organized has plainly forfeited its privileges; and there is but little difference in principle between the two cases. In both the corporation is actually in existence, but whether legally and rightfully so is the question. And it appears to me that if the court can take cognizance of the matter in this case, it must in all others where it can be brought up, not only directly, but incidentally."

This case is approved and followed in *National Docks R. Co. v. Central R. R. Co.*, 32 N. J. Eq. 755, which held: "When a corporation exists *de facto*, the court of chancery cannot, at the instance of private parties, restrain its operations upon the ground that its organization is not *de jure*. In such case the proper remedy is by *quo warranto*, or information in the nature thereof, instituted by the attorney-general." The rule of estoppel found no place in this case.

In *S. & L. G. R. Co. v. S. & C. R. R. Co.*, 45 Cal. 680, it was held that: "If a corporation *de facto* is in the actual possession of a public highway, under a grant of a franchise to improve and collect tolls on the same, a mere trespasser cannot justify his entry thereon on the ground that it was only a corporation *de facto*, and was not *de jure* entitled to the franchise."

In *Williams v. Kokomo B. & L. Ass'n.*, 89 Ind. 339, one Leach gave to an acting corporation his mortgage on real estate. Subsequent to the execution and recording of it, he executed another mortgage on the same land to Williamson. In a proceeding to foreclose the junior mortgage, Williamson maintained that the pretended corporation had no legal existence, by reason of defects and omissions in the proceedings to incorporate, and that the senior mortgage was void. He was in no manner estopped, by dealings with, or recognition of, the first mortgagee to deny its corporate existence. The court held that: "A junior mortgagee cannot defeat a senior mort-

gage by showing that the corporation to which the senior mortgage was executed was defectively organized, if it be a corporation *de facto*." Elliot, J., said: "Where persons assume to incorporate under the laws of the state, and in part comply with their requirements, assume corporate functions and transact business as a corporation, private persons cannot collaterally question the right of such an association to a corporate existence, although there has not been a full compliance with the provisions of the statute. *Baker v. Neff*, 73 Ind. 68. *This rule is not limited to cases where one by contract admits corporate existence, but is a rule of general application.*" It is not easy to distinguish the principle of this case from that of the case at bar.

In *Pape v. Capitol Bank*, 20 Kan. 440, Pape and wife gave their notes to "James M. Spencer or bearer," and their mortgage on real estate to secure them. Spencer transferred the notes to the Capital Bank of Topeka, an acting corporation, with this indorsement: "Pay the bearer, without recourse on me; James M. Spencer." The mortgage was also transferred to the bank, which proceeded by suit to collect the notes and foreclose the mortgage. Pape and wife interposed the defense that the bank was not, and never had been, a body corporate, by reason, among others, of a defective organization. The bank had assumed corporate functions after an attempt, in good faith, to incorporate, and for a number of years was in the actual and notorious exercise of corporate franchises. Pape had transacted banking business with the plaintiff prior to the purchase of the notes and mortgage, but such business was wholly unconnected with the notes and mortgage in suit. His wife, however, had not in any manner recognized the existence of the bank as a corporate body, and the doctrine of estoppel was not invoked to aid the court in sustaining a judgment of foreclosure against Pape and wife. Brewer, J., says: "The corporation is one *de facto*; and only the state can inquire, and that, in a direct proceeding, whether it be one *de jure*."
* * * There must, in such cases, be a law under which the incorporation can be had; there must, also, be an attempt, in good faith, on the part of the incorporators, to incorporate under such law; and when, after this, there has been for a series of years an actual, open, and notorious exercise, unchallenged by the state, of the powers of a corporation, one who is sued on a note held by such corporation will not be permitted to question the validity of the incorporation as a defense to the action. No mere matters of technical omission in the incorporation, no acts of forfeiture from misuser after the incorporation, are subjects of inquiry in such an action. *This is not upon the ground of equitable estoppel but upon grounds of public policy.* If the state, which alone can grant the authority to incorporate, remains silent during the open and notorious assertion and exercise of corporate powers, an individual will not, unless there be some powerful equity on his side, be permitted to raise the inquiry."

In *Thompson v. Candor*, 60 Ill. 244, Willetts, in February, 1858, deeded to "Mercer Collegiate Institute," a body pretending to be a

corporation, the tract of land in controversy. He died in March, 1858. In 1868 his heirs quitclaimed their interest in the land to Thompson, who filed a bill in chancery for the cancellation of the deed from Willetts to the "Institute," alleging, as one of the grounds of relief, that the named grantee was not legally incorporated—had no capacity to take the title, and that the deed was void. The court held:

"Where parties endeavor to organize a corporation for educational purposes, under the general law, adopt a name, elect trustees, and organize by electing a president and officers, and the trustees had acted for years in managing the property, had leased and mortgaged it, and expended a large sum of money in its improvement, these acts constitute it a corporate body *de facto*, and the regularity of its organization cannot be questioned collaterally. Such irregularity can only be questioned by *quo warranto* or *scire facias*."

Thornton, J., says: "In 1856 an attempt was made to organize a corporation under the general incorporation law. A corporate name was selected, trustees were appointed, and an organization effected by the election of a president and proper officers. The trustees thus appointed acted for years in the general management of the property, leased and mortgaged it, and expended a large amount of money. Here then was a corporate body *de facto*, which had been engaged in an undertaking involving important interests. The regularity of its organization cannot be questioned collaterally. Any alleged non-compliance with the law can only be inquired into by the writ of *quo warranto* or *scire facias*."

There is no suggestion throughout the entire case of the rule of estoppel as an element affecting its disposition.

In *Paper Works v. Willett*, 1 Robertson (N. Y. Sup.), 131, it is held that formal defects in proceedings to organize a corporation are not available to defeat an action brought by a corporation for trespass in wrongfully taking property out of its possession.

See also, as illustrating the principle under discussion: *Smith v. Sheeley*, 12 Wall. 361; *Grand Gulf Bank v. Archer*, 8 S. & M. 151, 173; *Dunning v. R. R. Co.* 2 Carter (Ind.) 437; *Dannebroge Mining Co. v. Allment*, 26 Cal. 286; *Searsburgh Turnpike Co. v. Cutler*, 6 Vt. 315; *Mitchell v. Deeds*, 49 Ill. 416; *Eliz. Academy v. Lindsey*, 6 Ired. 476; *Darst v. Gale*, 83 Ill. 136; *Rondell v. Fay*, 32 Cal. 354; *De Witt v. Hastings*, 40 N. Y. (Superior Court) 463; *Rice v. R. R. Co.*, 21 Ill. 93; *Douglas County v. Bolles*, 94 U. S. 104; *The Banks v. Poitiaux*, 3 Randolph (Va.), 136; *Goundie v. Northampton Water Co.*, 7 Pa. St. 233; *Baker v. Backus*, 32 Ill. 79; *Tarbell v. Page*, 24 Ill. 46; *Thornburgh v. R. R. Co.*, 14 Ind. 499; *Tar River Nav. Co. v. Neal*, 3 Hawks, 520; *Bear Camp River Co. v. Woodman*, 2 Me. 404.

In *Jones v. Dana*, 24 Barb. 395, it was held that if a company has in form a charter authorizing it to act as a body corporate, and is in fact in the exercise of corporate powers at the time of taking a note from an individual, it is, as to him and all third persons, a corpora-

tion *de facto*, and the validity of its corporate existence can only be tested by proceedings on behalf of the people.

In the case, at bar, the certificate which was last filed by the society embraced a full statement of the objects of incorporation and indicated what the nature of its business must necessarily be, and was strongly suggestive of the manner in which it must necessarily be transacted; and while it is not our purpose to call in question the action of this court in the quo warranto proceedings, we have no hesitation in saying that if we were now called upon to determine whether the corporate life of Society Perun should be taken, the question, upon the facts offered in proof at the trial below, would not be free from doubt and difficulty. It is very clear that the proceedings to incorporate were colorable; and so far as this fact is a test of the existence of a corporation *de facto*, it is most amply established. That there was proof of user is manifest from the evidence which was received without objection.

That the judgment of ouster did not and could not have a retroactive effect upon the rights of the society, and of parties who had dealt with it during its *de facto* existence, is suggested by the opinion of Wright, J., in *Gaff v. Flesher*, 33 Ohio St. 115.

The evidence which was offered and excluded would, if credited, have shown Society Perun capable of holding and transferring the legal title to the land in controversy. *Walsh v. Barton*, 24 Ohio St. 43; *Darst v. Gale*, 83 Ill. 136; *Shewalter v. Pirner*, 55 Mo. 218; *Nat. Bank v. Atthews*, 98 U. S. 628; *Goundie v. Northampton Water Co.*, 7 Penn. St. 233; *Barrow v. Nashville Turn. Co.*, 9 Humph. 304; *Kelly v. People's Trans. Co.*, 3 Ore. 189; *Bogardus v. Trinity Church*, 4 Sandf. Ch. 758.

The public and all persons dealing with this society were justified in assuming that the certificate filed with the secretary of state, and by him admitted to record in his office, had been approved by him, and also by the attorney-general, as required by statute (69 Ohio L. 150), and that it so far conformed to all legal requirements that, as provided in section 2 of the act of incorporation (69 Ohio L. 83), "a copy, duly certified by the secretary of state, under the great seal of the state of Ohio, shall be evidence of the existence of such association."

It would seem that such approval, record, and certificate, followed by uninterrupted and unchallenged user, for nearly six years, of all of which proof was tendered, would constitute a corporation *de facto*, if such a body is, under any circumstances, entitled to legal recognition.

The highest considerations of public policy and fair dealing protest against treating such an organization as a nullity, and all of its transactions void.

The principle of the above cases is to be distinguished from a case where a mere corporation *de facto* attempts to assert the power of eminent domain by the appropriation of private property to public use. It has been held that the exercise of this right (which is but a

delegation of the sovereign power of the state), depends upon the sufficiency and legal validity of the certificate of incorporation and public record of its organization. *R. R. Co. v. Sullivant*, 5 Ohio St. 276; *Atkinson v. R. R. Co.*, 15 Ohio St. 21.

The case of *Raccoon River Nav. Co. v. Eagle*, 29 Ohio St. 238, is relied upon by the defendant in error. It was an action to recover upon a stock subscription. A plea of *nul tiel corporation* was interposed. The plaintiff claimed to be organized under an act to authorize the incorporation of companies "for the purpose of improving any stream of water * * * declared navigable by any law of the state of Ohio." On the trial the plaintiff offered in evidence a certificate by which it appeared that the company was formed for the purpose of improving, etc., Big Raccoon river. Unfortunately there was no navigable stream in Ohio by that name. No other testimony was offered. There was no proof of user. There was no defect in the form of the proceedings to incorporate, but an attempt to organize and incorporate for a purpose impossible of accomplishment. There was neither a *de jure* nor *de facto* corporation. Judgment was properly rendered for defendant.

In excluding proof of what was actually done looking to the incorporation of Society Perun, and of the subsequent acts of user, which was offered in evidence, there was error, for which the judgment in the first entitled case (as well as that in the same plaintiff against *Hay et al.*, which was tried with it and involves the same general questions) is reversed. Numerous other questions are presented by the voluminous records in these cases, but as they all depend upon the one central and controlling question discussed above, and as the disposition here made of the cases must lead to a re-trial in the light of the principles indicated in this opinion, they are not separately considered.

*Judgment reversed.*¹³

FOSTER v. MOULTON.

1886. 35 Minn. 458, 29 N. W. 155.

APPEAL by defendant E. H. Moulton from an order of the district court of Blue Earth county, Severance, J., presiding, overruling his separate demurrer to the complaint.

BERRY, J.—The complaint in this action sets out what purports

¹³ *Finch v. Ullman* (1891), 105 Mo. 255, 16 S. W. 863, *Accord*.

Under a prosecution for embezzlement from an "incorporated company," held that it sufficed to show that the money taken was the property of a *de facto* corporation. *People v. Carter* (1900), 122 Mich. 668, 81 N. W. 924. And so, *Brewer v. State* (1881), 7 Lea (Tenn.) 682.—Eds.

to be the articles of incorporation of a mutual benefit association, which appears to have been intended to be a sort of mutual insurance company, and alleges that said articles were duly executed by defendants, and duly recorded with the register of deeds and secretary of state; that one McCarthy became a member of the association, paid his dues, and received a certificate of membership; that he sustained bodily injury entitling him, as such member, to pecuniary benefit; that the amount due him under the terms of his membership has not been paid; and that he has duly assigned his right to such benefit to the plaintiff.

The association did not comply with the statute so as to become an insurance corporation *de jure*. The appellant (one of the defendants) contends that it was duly incorporated as a benevolent society under Gen. St. 1878, ch. 34, title 3. This cannot be so, for it is no more a benevolent society than any mutual insurance company, or other mutual company, or any partnership of which one member undertakes to do something for the pecuniary advantage of another member, in consideration of the undertaking of the latter to do a like thing for him. The undertaking is not in any proper sense *benevolent*, but it is for a *quid pro quo*; it is paid for. *People v. Nelson*, 46 N. Y. 477. The association involved in the case at bar is, in substance, for purposes of *mutual insurance*. *State v. Merchants' Exch. Mut. Benev. Soc.*, 72 Mo. 146; *State v. Benefit Ass'n*, 6 Mo. App. 163; *Com. v. Wetherbee*, 105 Mass. 149; *May, Ins.*, § 550a.

But notwithstanding it is not a corporation *de jure*, we think it must, at least, as between its members, be regarded as a corporation *de facto*. It is manifest that the understanding between the members, and the basis upon which certificates of membership were issued, was that the association was a corporation in fact as it was in form. *Morawetz, Priv. Corp.*, § 139. It never could have been intended or expected that the members of the association, whether original founders,—members like defendants,—or those who should become members by joining at any time, should or would be liable as individuals, either jointly or severally, to any particular member who should, by virtue of and under the terms of his membership, become entitled to pecuniary relief or benefit. On the contrary, the intention and the real contract was that the association, as a corporation in the contemplation of the parties, *i. e.*, the members, should be liable, and the association only. In such a state of facts, though the association is not a corporation *de jure*, and perhaps not for every purpose a corporation *de facto*, it is, as between the members themselves, to be treated as a corporation *de facto*, (for that is the way in which the *contract* of the parties treats it;) and the right of a member to pecuniary benefit from the association by virtue of his membership must stand upon the basis that it is a corporation *de facto*. Being presumed to know the significance of his membership, its rights and liabilities, (*Coles v. Iowa State Mut. Ins. Co.*, 18 Iowa, 425,) he is estopped to take any other position. This is not only intrinsically just and fair, but it is in accordance with the principles

of the authorities. *Morawetz, Priv. Corp.*, §§ 131, 132, 134-137; *Buffalo & A. R. Co. v. Cary*, 26 N. Y. 75, followed in 57, 64, 67, N. Y., and 95 U. S.; *White v. Ross*, 4 Abb. Dec. 589; *Aspinwall v. Sacchi*, 57 N. Y. 331; *Eaton v. Aspinwall*, 19 N. Y. 119; *Sands v. Hill*, 46 Barb. 651; *Sanger v. Upton*, 91 U. S. 56; *Chubb v. Upton*, 95 U. S. 665.

It is important to bear in mind that no fraud is alleged against defendant; and, further, that this is a case in which a member of the association is seeking relief by virtue of his membership. If the action were between a purported or pretended corporation, which was wholly unauthorized and invalid, and a stranger, different rules and principles might, in some circumstances, be involved.

The application of the foregoing views is that, the action having been brought against defendants as individuals merely, the general demurrer of the appellant, who was one of the defendant members of the association, was erroneously overruled. The overruling order is accordingly reversed.¹⁴

¹⁴ *Bushnell v. Consolidated Ice Machine Co.* (1891), 138 Ill. 67, 27 N. E. 596; *Anderson v. Thompson* (1899), 51 La. Ann. 727, 25 So. 399; *Casanas v. Audubon Hotel Co.* (1909), 124 La. 786, 50 So. 714, *Accord.* See *Common v. McArthur* (1898), 29 Can. Sup. Ct. 239.—Eds.

CHAPTER IV.

POWERS OF A CORPORATION.

Section 1.—In General.

10 Co. 30 b. That when a corporation is duly created, all other incidents are tacite annexed. And for direct authority in this point in 22 E. 4, Grants 30, it is held by Brian, Chief Justice, and Choke, that corporation is sufficient without the words to implead and to be impleaded, and therefore divers clauses subsequent in the charters are not of necessity, but only declaratory, and might well have been left out. As 1. By the same to have authority, ability and capacity to purchase, but no clause is added that they may alien, etc., and it need not, for it is incident. 2. To sue and be sued, implead and be impleaded. 3. To have a seal, etc., that is also declaratory, for when they are incorporated, they may make or use what seal they will.

ATTORNEY-GENERAL v. MERSEY RAILWAY CO.

1906. L. R. (1907) 1 Ch. Div. 81. 1907. L. R. (1907) A. C. 415.¹

APPEAL from a decision of Warrington, J.

The action was brought by the Attorney-General at the relation of the corporation of Birkenhead, and by the corporation, against the Mersey Railway Company, for a declaration that it was beyond the powers of the railway company to carry on the business of omnibus proprietors in the borough of Birkenhead, and for an injunction to restrain them from so doing. The defendant company owned and worked a railway which connected Liverpool and Birkenhead by means of a tunnel under the river Mersey. After passing beneath the river the railway ran into Hamilton Station in Birkenhead and then divided into two branches, one of which went northwest to Park Station and the other southeast to Central Station and then south to Green Lane and Rock Ferry Stations. All these stations were in the borough of Birkenhead. The traffic on their line was mainly a passenger traffic. The corporation owned and worked a ferry across the river Mersey, and they also owned and worked a system of electric tramways in the borough of Birkenhead. These tramways connected the riverside with the distant and more hilly parts of the town,

¹ Some of the opinions are omitted.—Eds.

which constituted the residential quarter, and from which a large portion of the passenger traffic of the railway and the ferry was alike derived. The corporation ran their cars at intervals of ten minutes, and during the greater part of the day the cars passed the Central Station of the defendant company; but during certain portions of the day they took an alternative route which led directly to the ferry without passing the defendants' station, and the defendants were thereby placed at a great disadvantage in competing with the corporation for the traffic between Liverpool and Birkenhead. Accordingly, in the autumn of 1905, the defendants applied to the corporation, as the licensing authority, under the Birkenhead Corporation Act, 1881, (44 and 45 Vict., chap. cliii), and the Town Police Clauses Acts, 1847 and 1889, (10 and 11 Vict., chap. 89, and 52 and 53 Vict., chap. 14), to license six motor omnibuses to ply for hire as hackney carriages within the borough. The corporation granted the licenses, but without prejudice to their right to take any further steps in the matter. In December, 1905, the defendant company instituted a service of motor omnibuses in connection with their train service, running every six minutes from 8 a. m. to 7. 30 p. m. between their Central Station and the residential portion of the town. These omnibuses picked up passengers along the road or at specific stopping places, and conveyed them to such other places on their route as the passengers might desire, and separate fares were fixed for journeys between intervening stopping places on the line of route. In all cases, however, the complete routes of these omnibuses either commenced or ended at the Central Station. The defendants had no express power under their special acts to run omnibuses in connection with their trains.

WARRINGTON, J., held that it was ultra vires of the defendant company to carry on the business of omnibus proprietors, and granted the injunction.

The railway company appealed.

BUCKLEY, L. J.—We have here to deal with a statutory corporation. The general rule is that a chartered company can do anything which is not by its charter forbidden, but that a statutory corporation can do only that which is by its statute authorized. The chartered corporation is a corporation at common law. The statutory corporation is not. The latter owes its existence wholly to the statute and cannot go beyond the statute which creates it. The statute, however, in many cases defines only the purpose; sometimes it also defines special powers. But, whether in the one case or the other, the statutory corporation is not by the general principle above stated restricted to acts specifically mentioned or referred to in the statute. To ascertain whether any particular act is ultra vires of the statutory corporation or not the main purpose must first be ascertained; then the special powers for effectuating that purpose must be looked for, and then, if the act is not within either the main purpose as described in or the special powers expressly given by the statute, the inquiry re-

mains whether the act is incidental to or consequential upon the main purpose and is a thing reasonably to be done for effectuating it. To quote Lord Selborne in *Attorney-General v. Great Eastern Ry. Co.* (2), the doctrine of ultra vires is to be reasonably and not unreasonably understood and applied, and whatever may fairly be regarded as incidental to or consequential upon those things which the legislature has authorized ought not (unless expressly prohibited) to be held by judicial construction to be ultra vires. By way of illustration, let me suppose that the main purpose found in the statute or in the memorandum of association of a statutory company is to establish and carry on an hotel, and that express power is given to buy land at a particular place and to build, and that as to anything further the statute or memorandum of association is silent. It is quite clear law that all such acts as are reasonably necessary for effectuating that purpose are intra vires, such, for instance, as the purchase of furniture, and of linen, of provisions, and of wines and spirits, the hiring of servants, the payment of licenses, the ownership probably of horses and carriages, the maintenance and working of an omnibus which shall attend at the railway station to take intending guests to the hotel and the like. In a large number of cases the maintenance of a garden and pleasure grounds would be intra vires. The legitimate extent of these would depend upon circumstances. The maintenance of tennis lawns or of a bowling green would in many circumstances, be legitimate. Under circumstances such as presently put a golf links might be intra vires. All these and the like will without express mention be within the company's powers. Then I may instance other acts as to which it would be a question of fact in the case of the particular hotel whether it was such an act as would be reasonably incidental or consequential. If, for instance, the hotel were at Bundoran or Rosapenna or elsewhere in the county Donegal it might be intra vires to lay out and maintain in good order a golf links or to acquire rights of fishing and to own boats and to supply gillies for the purpose of fishing upon the lakes. It may be that in the particular locality custom could only be reasonably expected or obtained by offering those attractions, and they might be as necessary as a smoking-room or a bowling green elsewhere. If the hotel in question were the Savoy Hotel in the Strand or the Great Central Hotel in the Marylebone Road the proposition would cease to be true. So, again, if the hotel were situate in a place inaccessible unless special means of communication were provided—say, at a lovely spot at the end of the Scotch Loch to which there is no road, or at a place to which there is access by a road but which is not served by any coach or mail cart service—it might be intra vires for that hotel to run a steam launch or a motor car to bring its guests to their destination. It would in such a case be analogous to the omnibus which the hotel in the country town sends to the railway station. The question is in each case a question of fact, Is the particular act as to which it is in question whether it is

intra vires an act which in the circumstances of that particular case is incidental to or consequential upon or reasonably necessary for effectuating the main purpose which the statute defines?

The learned judge below has dealt with this case as if the decision of this court and of the House of Lords in the *Attorney-General v. London County Council* (1) concluded it. In that case, as it appears to me, two matters came in question, and upon the decision of these the case turned. They were, first, the true construction of s. 2 of the *London County Tramways Act, 1896*, (59 and 60 Vict., c. li.) and, secondly, whether the omnibus business there carried on was a separate business or was one incidental or ancillary to the tramway business. Upon the former of these it was held that the *London County Council* could only purchase tramway undertakings as contrasted with omnibus undertakings. The vendor to the *London County Council* owned both a tramway undertaking and an omnibus undertaking. The good will of the omnibus undertaking was excluded from the sale. The first point was that, as a matter of construction of the act, the *London County Council* was excluded from the omnibus business. "The power" (said Lord Halsbury) "which is expressly given to the *London County Council* excludes from them, and to my mind is intended to exclude from them, that which did exist as a separate business under the earlier statute, and which was not intended, and obviously was not intended, to be conferred upon the *London County Council*." Rigby, L. J., in this court had said: "If the intention was, and if parliament was disposed to accede to it, that the county council should take over and work the whole of the company's undertaking, including both branches, namely, the tramway branch and the omnibus branch, it would have been easy to say so in section 2 of the *London County Tramways Act, 1896*. Nothing of the sort is said, and it is admitted that there is nothing in the section which clearly and specifically refers to a transfer of the whole undertaking and power to run both tramways and omnibuses." Vaughan Williams, L. J., pointed to the same consideration, and in the court below Cozens-Hardy, J., had emphasized the same point. The second question was a question of fact, namely, whether the omnibus business was a separate business. It was held that it was. If this be the true effect of that case, it, of course, does not relieve me from investigating whether upon the state of facts in this case the business is really a separate business or is only one incidental to the main business. From the fact that it was a separate business there it does not follow that it is a separate business here.

Let me first see as a general question whether the ownership and running of omnibuses for the convenience of passengers can be said to be without qualification *ultra vires* of this railway company. The order below has affirmed that it is. The order declares that it is beyond the powers of the defendant company to run or work omni-

(1)—(1902) App. Cas. 165.

buses for the purpose of carrying passengers in any of the streets within the borough of Birkenhead. This would preclude the defendant company from supplying for the use of passengers a private omnibus hired by the passenger to take him from or to the station. Nobody has advanced that as a proposition which can be supported. In my opinion it is impossible to support it. A reasonable service to be rendered to the passenger to enable him to make his journey complete is no more as a general proposition *ultra vires* than is the service of a porter to wheel his luggage to a cab or according to circumstances, say, at Crianlarich, on the West Highland Railway, to the neighbouring station of another railway. The order below is, at any rate, too wide.

Then, secondly, if railway companies may own and run omnibuses for some purposes, may they *bona fide* run omnibuses which are not let to a single particular hirer, but which stand at the station to take up passengers at separate fares and convey them by a definite route at any point of which the passenger may alight? I cannot see how this in principle differs from the first case. There is no magic in a single hirer as distinguished from several passengers at separate fares. The omnibus in that case would, I think, be a facility offered to passengers, and the act would be one reasonably to be done for effectuating the purpose of developing the traffic of the railway.

Thirdly, suppose the omnibus is traveling to the station as an omnibus available to take passengers at separate fares. In such case, there is an obvious difficulty in knowing whether the passenger who hails the omnibus is going to the station or not. If the omnibus be really run as an omnibus to the station, it does not, I think, lose that character by reason of the fact that persons may claim to be passengers in the omnibus who turn out afterwards not to be passengers on the railway.

Lastly, suppose that the omnibus which starts from the station takes up passengers in the streets on its journey, does this make the running of the omnibus *ultra vires*? This is, I think, a question of degree. If I arrive at the conclusion that as a matter of fact the service of the omnibus is *bona fide* supplied for the use of persons who have been or who are going to be passengers on the railway, its employment does not become *ultra vires* because in use as a commercial matter passengers are not refused whose conveyance will add something to the profits or diminish something of the loss upon the working of the omnibuses.

A good deal of discussion has taken place as to whether the company can obtain the license of the corporation to run omnibuses except upon the terms that they shall be bound to take any person on their route who wishes to be a passenger and pays his fare. I think it unnecessary to form any concluded opinion as to whether this is an obligation or not. If it be an obligation so that they cannot run omnibuses *bona fide* for the purposes of their railway without performing it, then I think it cannot render the act *ultra vires* if they submit

to that necessity when, as I find to be the fact, this will be only an adventitious and not a principal service. If, on the other hand, they are not bound to come under the obligation, I think, as above stated, that if the omnibus is really for the purposes of the railway, the act does not become ultra vires by their taking to a reasonable extent extraneous traffic which adds something to the commercial prosperity of the undertaking. Upon the authorities a corporation may reasonably use its property in such a manner for purposes not forming part of its main purpose. I may mention by way of illustration, taking them in order of date, *Simpson v. Westminster Palace Hotel Co.* where a portion of the hotel in the course of being built was let off for a time for a government department; *Forrest v. Manchester, Sheffield and Lincolnshire Ry. Co.*, where steam vessels, kept for the purposes of a ferry, were employed, when not wanted for that purpose, for excursion trips on the sea; *London and North Western Ry. Co. v. Price & Son*, where the railway company allowed its weighing machine to be used for hire for weighing some one else's coals; and *Foster v. London, Chatham and Dover Ry. Co.*, where a railway company let its arches for shops.

In my judgment, therefore, the decision of the present case must be simply a decision of this question of fact, Are the defendants really running the omnibuses here in question for the purpose of their railway and so as to obtain and give facilities for better traffic over their line, or is the omnibus business really an independent business in which they look substantially to general street traffic? Upon this question of fact the decision of *London County Council v. Attorney-General* is not conclusive nor even necessarily applicable. My great difficulty in the matter arises from the fact that the evidence is so exceedingly meager. The material facts, so far as I know them, are these: That the railway company is one whose undertaking is substantially a short line running under the Mersey between Birkenhead and Liverpool, and its service of trains is a service at six-minute intervals, that the omnibuses in question are also run at six-minute intervals so as to connect with the trains, that they run exclusively from and to the central station, that on the omnibuses appears prominently the statement that the omnibus runs to and from the Mersey railway station, that the service ceases in the evening about 7:30 or 8:00 o'clock, when the Birkenhead residents, for whom the service is especially intended, have mostly returned to their homes—a fact which seems to indicate that the defendants do not lay themselves out for general street traffic, such as traffic to the theaters or the like. To the above facts I add that the interest of the defendants is to prefer such persons as have been or are going to be passengers on their line, and, so far as they have any power of selection, their interest must be to take such members of the public as are, rather than those that are not, going to travel on the railway. To the above I add this fact, that the plaintiffs and relators in the action, the corporation of Birkenhead, are the owners of a rival means of crossing the Mersey, viz.,

a ferry, and are the owners of a system of tramways which are convenient for that ferry and not convenient for the defendants' railway. In the circumstances it was in my judgment a reasonable course that the defendants should seek to obtain their proper share of the traffic by giving facilities for reaching their railway, having regard to the facilities which the corporation enjoyed for attracting the traffic to the corporation's ferry. On the other side I have the fact that there are fares charged in two cases between points neither one of which is the central station. Upon these facts I arrive at the conclusion of fact that the defendant did really bona fide establish this system of omnibuses for the purpose of obtaining traffic on their railways; that the omnibuses are, so far as the defendants can insure it, intended to be incidental to their railway and are reasonably wanted to effectuate the purpose of bringing to their railway the traffic or a fair proportion of the traffic. Thus answered the question is resolved in favor of the defendants.

The defendants are prepared to abandon the separate fares for persons traveling between points neither of which is the central station, which I will call outlying fares, and to give an undertaking that they will in future make all fares charged upon their omnibuses fares to or from some one of their stations, to the exclusion of fares to or from places neither one of which is such a station. This undertaking removes one matter which rather pressed upon the court, viz., that the railway company might by these outlying fares be holding themselves out as seeking general street traffic, and another matter, viz., that if passengers at these outlying fares became proportionately numerous, a business which I think at present intra vires might develop into one which would be ultra vires. Upon this undertaking being given, I think the injunction granted below should be discharged.

VAUGHAN WILLIAMS, L. J.—I want to say this in respect of the judgment which I have delivered. There are a few words which I should like to add, and I have asked Buckley, L. J., whether he sees any objection, because in a sense they refer to a matter referred to in his judgment, and he says he has no objection to my adding these words to my judgment to put it right. That is this: You ought to give a wider construction to the words of a memorandum of association creating and defining the powers of a purely commercial company having no compulsory powers and no monopoly than you would give to the words of a statute creating a company, like the railway company, having compulsory powers of land purchase and a practical monopoly.

December 14. After some discussion the court made the following order (BUCKLEY, L. J., dissenting as to the costs):—

The defendants undertaking (1) to run their omnibuses to or from a railway station upon their line and in connection with trains upon their railway, and not otherwise, and to so advertise their omnibus service, and not to advertise or hold themselves out as carrying on a

general omnibus business or as carriers of passengers in their omnibuses otherwise than to or from one of their railway stations; (2) to make all fares charged in respect of their omnibus service fares to or from some one of their stations, and not to make or charge any separate fare between places neither of which is such a station; (3) to run their omnibus service as a service for railway passengers, and as far as reasonably practicable to confine their service to passengers to or from some one of their stations, discharged the injunction, but without disturbing the order of the court below as to costs. No order as to the costs of the appeal.

From the above order the attorney-general appealed to the House of Lords.

LORD LOREBURN, L. C.—My Lords, in this case the question is whether a railway company is entitled to run a number of omnibuses which it says are incidental to the railway enterprise itself. The rule of law has been laid down in this House to the effect that it must be shewn that the business can fairly be regarded as incidental to or consequential upon the use of the statutory powers; and it is a question in each case whether it is so, or whether it is not so. In the present instance I do not think that this business of running an omnibus system can be regarded incidental to or consequential upon the statutory enterprise. It seems to me that in substance it was an undertaking for the purpose of enabling the railway company successfully to compete with the ferry which belonged to others.

It is unnecessary to elaborate the distinctions between this and other cases that have been quoted because I do not believe that much assistance is derived by reasoning from analogy when the question at issue is in substance either a question of fact or at least a mixed question of fact and law. I agree with the judgment given by Warrington, J., who granted an injunction. The Court of Appeal have limited the injunction, or, what is the same thing, have refused the injunction, but required an undertaking. In my view that undertaking is one which could not be carried out in a business sense; and I think it involves the admission that, under restrictions such as are included in the undertaking, this business would be *intra vires*. I am of opinion that the order appealed from should be reversed.

LORD MACNAGHTEN.—* * * The principle to be applied is perfectly clear. The difficulty is all in the application. Hundreds of cases may be suggested where the thing done comes very near the line and may fairly be open to a difference of opinion. Speaking for myself, I cannot see what is to be gained by discussing such cases, real or imaginary, however interesting the discussion may be. Here, I think, the respondents have transgressed the line. It may be that in doing what they wish to do they cannot help it. But that, in my opinion, is no justification for their action. If they wish to extend their undertaking beyond the limits authorized by their charter, the proper course is to apply to Parliament for further powers.

LORD JAMES, of Hereford.—My Lords, I desire to add a few observations. It seems to me that we have to look at the state of circumstances that existed upon December 23, 1905, when the relators instituted this action, and to determine whether at that time the allegation which was made that the defendants carried on the business of omnibus proprietors and ran, plied for hire, or worked the omnibuses for the purpose of carrying passengers in the streets of Birkenhead, was or was not proved. Whatever has occurred since by way of modification of the business, I do not think, ought to govern this case at all, and therefore the terms made in the Court of Appeal cannot now be regarded as controlling this action. If by those modifications the defendants have brought themselves within their powers, they need no undertaking, they wanted no authority; they would raise no cause of action. If they have not done so, they have only maintained the state of things that existed in the month of December, 1905.

Now, My Lords, I am rather anxious to say that I do not think it is the intention of your Lordships in any way to prevent railway companies considering the convenience of their customers, the persons whom they are carrying. No doubt, there are certain things incidental to the carriage of passengers which can be done. Of these, perhaps that which is most attractive would be the giving of refreshments on the line. That is not, I presume, authorized in express terms by the statutes, but that is incidental to the carriage of passengers. In the same way the meeting of passengers or delivering them at their places of abode, where they wish to go, by an omnibus, may well be carried on without exceeding the statutory powers. But, My Lords, in this case that was not what existed at the time this action was brought. Here, as we see if reference be made to the plan which has been called the "STAR" plan, it is proved that the course of the omnibus was to cling, as it were, to the tramways as competitors with the tramways, and to take passengers by these omnibuses who would otherwise have gone by the Birkenhead Tramways. It was not confined to dealing with the passengers on the railway; it was an open omnibus business, picking up wherever they could find passengers for the profit of the omnibuses, and not for the convenience of the railway passengers.

Therefore, My Lords, it seems to me that this case is taken outside of all those cases that have been mentioned where, incidental to the business of the railway company or any other company, business was carried on that was not specially mentioned in the statutory powers, and that this was an independent business that was attempted to be carried on by this company.

My Lords, the danger of accepting the argument of the defendants is, that the natural consequence would be to give a railway company power to carry on a business as a railway company which they never had the power to carry on, because, if bringing passengers as feeders to a railway is incidental to that railway company's business,

it would not be confined to bringing them by omnibuses; you may bring them by tramways or by tramcars or by cars moved by locomotive steam power; and that would be simply an extension of the railway. If the railway company could overcome the difficulty of taking land without compulsory powers, if they could take land by agreement, they would be able to bring into existence new railways not authorized by statute, and, I presume, be entitled to impose their own terms and tolls, unregulated by legislative control, if they thought fit. That would be a principle which your Lordships would be very slow to sanction or approve. And I think if the course which my noble and learned friend on the woolsack has moved should be taken is not taken, the result would be to extend the power of railway companies in a most dangerous manner.

*Order reversed.*²

JACKSONVILLE, ETC., RAILWAY & NAVIGATION
CO. v. HOOPER.

1895. 160 U. S. 514, 40 L. ed. 515, 16 Sup. Ct. 379.³

IN the Circuit Court of the United States for the northern district of Florida, on the 4th day of December, 1889, Mary J. Hooper, Henry H. Hooper, her husband, and William F. Porter, for the use of said Mary J. Hooper, citizens of the state of Ohio, brought an action against the Jacksonville, Mayport, Pablo Railway and Navigation Company, a corporation of the state of Florida. The plaintiffs' amended declaration set up causes of action arising out of the covenants contained in a certain indenture of lease between the parties. This lease, dated July 10, 1888, purported to grant, for a term of two years, certain lots of land situated at a place called "Burnside," in Duval County, Florida, whereon was erected a hotel known as "San Diego Hotel." In consideration of this grant the railroad company agreed to pay in monthly instalments a yearly rent of \$800, and to keep the premises insured in the sum of \$6,000.

²London County Council v. Attorney-General (1902) App. Cas. 165, *Accord*. See also Attorney-General v. Great Eastern R. Co. (1880) 5 App. Cas. 473; People v. Pullman's Palace Car Co. (1898) 175 Ill. 125, 51 N. E. 664 (elaborate discussion of implied powers).

In considering the appropriate construction of the memorandum and articles of association of a corporation, Bacon, V. C., said: "I wholly repudiate the notion that I am at liberty to adopt what has sometimes been called a 'liberal' construction. I have no more right to do that on the one hand than I am at liberty on the other to adopt a more rigorous or more strict construction than the express stipulations of the instruments require. What the law requires and what I am called upon to do is to put a just construction, and no other, upon these instruments." London Financial Assn. v. Kelk (1884) 26 Ch. Div. 107, at page 134. *Accord*, Downing v. Mt. Washington Road Co. (1860) 40 N. H. 230.—Eds.

³Portions of opinion omitted.—Eds.

It was alleged that on November 28, 1889, during said term, and while the railway company was in possession, the hotel and other buildings were wholly destroyed by fire; that the defendant had failed and neglected to have the same insured, and that there was an arrearage of rent due amounting to the sum of \$106.67. For the amount of the loss occasioned by the absence of insurance and for the back rent the action was brought.

The defendant denied that the railway company had duly executed the instrument sued on; denied that Alexander Wallace, the president of the company, and who had executed the lease as such president, had any authority from the company so to do. The defendant also alleged that such a lease even if formally executed, was ultra vires; also that the covenant to insure was an impossible covenant, as shown by ineffectual efforts to secure such insurance.

The case was tried in April, 1891, and resulted in a verdict and judgment against the defendants in the sum of \$6,798.70. On errors assigned to certain rulings of the court and in the charge to the jury the case was brought to this court.

SHIRAS, J. * * * It is, however, further claimed that the contract sued on was not within the legitimate powers of the company.

This is not a case in which, either by its charter, or by some statute binding upon it, the company is forbidden to make such a contract. Indeed, the public laws of Florida, referring to the powers of railroad companies, provide that every such corporation shall be empowered "to purchase, hold, and use all such real estate and other property as may be necessary for the construction and maintenance of its road and canal and the stations and other accommodations necessary to accomplish the objects of its incorporation, and to sell, lease, or buy any land or real estate not necessary for its use." McClell. Digest of the Laws of Florida, page 276, section 10. They are likewise authorized "to erect and maintain all convenient buildings, wharves, docks, stations, fixtures, and machinery for the accommodation and use of their passenger and freight business."

Although the contract power of railroad companies is to be deemed restricted to the general purposes for which they are designed, yet there are many transactions which are incidental or auxiliary to its main business, or which may become useful in the care and management of the property which it is authorized to hold, and in the safety and comfort of the passengers whom it is its duty to transport.

Courts may be permitted, where there is no legislative prohibition shown, to put a favorable construction upon such exercise of power by a railroad company as is suitable to promote the success of the company, within its chartered powers, and to contribute to the comfort of those who travel thereon. To lease and maintain a summer hotel at the seaside terminus of a railroad might obviously increase the business of the company and the comfort of its passengers, and be within the provisions of the statute of Florida above cited, whereby a railroad company is authorized "to sell, lease, or buy any land

or real estate not necessary for its use," and to "erect and maintain all convenient buildings * * * for the accommodation and use of their passengers."

Courts may well be astute in dealing with efforts of corporations to usurp powers not granted them, or to stretch their lawful franchise against the interests of the public. Nor would we be understood to hold that, in a clear case of the exercise of a power forbidden by its charter, or contrary to public policy, a railroad company would be estopped to decline to be bound by its own act, even when fulfilled by the other contracting party. *Davis v. Old Colony Railroad Co.*, 131 Mass. 258; *Thomas v. Railroad Co.*, 101 U. S. 71; *Central Transportation Co. v. Pullman's Car Co.*, 139 U. S. 24. So, too, it must be regarded as well settled, on the soundest principles of public policy, that a contract, by which a railroad company seeks to render itself incapable of performing its duties to the public, or attempts to absolve itself from its obligation without the consent of the state, is void and cannot be rendered enforceable by the doctrines of estoppel. *The New York & Maryland Railroad Co. v. Winans*, 17 How. 30; *Thomas v. Railroad Co.*, 101 U. S. 71; *Central Transportation Co. v. Pullman's Car Co.*, 139 U. S. 24.

We do not seek to relax but rather to affirm the rule laid down by this court, in *Central Transportation Co. v. Pullman's Car Company*, (above cited,) that "a contract of a corporation, which is ultra vires, in the proper sense, that is to say, outside the object of its creation as defined in the law of its organization, and, therefore, beyond the powers conferred upon it by the legislature, is not voidable only, but wholly void, and of no legal effect—the objection to the contract is not merely that the corporation ought not to have made it, but that it could not make it. Such a contract cannot be ratified by either party, because it could not have been authorized by either. No performance on either side can give the unlawful contract any validity, or be the foundation of any right of action upon it." 139 U. S. 59, 60.

But we think the present case falls within the language of Lord Chancellor Selbourne, in *Attorney-General v. Great Eastern Railway*, 5 App. Cas. 473, 578, where, while declaring his sense of the importance of the doctrine of ultra vires, he said: "This doctrine ought to be reasonably, and not unreasonably, understood and applied, and that whatever may fairly be regarded as incidental to, or consequential upon, those things which the legislature has authorized, ought not, unless expressly prohibited, to be held, by judicial construction, to be ultra vires." In the application of the doctrine the court must be influenced somewhat by the special circumstances of the case. As was said by Romilly, M. R., in *Lyde v. Eastern Bengal Railroad*, 36 Beav. 10, where was in question the validity of a contract by a railway company to work a coal mine: "The answer to this argument appears to me to depend upon the facts of each particular case. If, in truth, the real object of the colliery was to supply the railway with cheaper coals, it would be proper to allow the accidental additional

profit of selling coal to others; but if the principal object of the colliery was to undertake the business of raising and selling coals, then it would be a perversion of the funds of the company, and a scheme which ought not to be permitted, however profitable it might appear to be. The prohibition or permission to carry on this trade would depend on the conclusions which the court drew from the evidence."

The principle upon which we may safely rule the present question is within the case of *Brown v. Winnisimmet Company*, 11 Allen, 326, 334. There a contract, made by the treasurer of a ferry company, to lease one of the company's boats for a certain money consideration, was alleged to be void for want of antecedent authority given by the company to the treasurer, and also because such a contract was not made in the legitimate exercise of the company's powers. On the first point it was ruled that, from evidence showing ratification by the company, it was proper for the jury to infer that the treasurer had been duly authorized to make the contract, and, disposing of the second question, the court, through Chief Justice Bigelow, said: "We know of no rule or principle by which an act, creating a corporation for certain specific objects, or to carry on a particular trade or business, is to be strictly construed as prohibitory of all other dealings or transactions not coming within the exact scope of those designated. Undoubtedly the main business of a corporation is to be confined to that class of operations which properly appertain to the general purposes for which its charter was granted. But it may also enter into and engage in transactions which are incidental or auxiliary to its main business, which may become necessary, expedient, or profitable in the care and management of the property which it is authorized to hold under the act by which it was created." See also, *Davis v. Old Colony Railroad*, 131 Mass. 258, 272.

The contract between the parties hereto was for leasing a hotel at the terminus of the railroad, situated at a beach, distant from any town. If not fairly within the authority granted by the statute of Florida "to erect and maintain all convenient buildings * * * for the accommodation and use of their passengers," it certainly cannot be said to have been forbidden by such laws. Nor can it be said to have been, in its nature, contrary to public policy.

To maintain cheap hotels or eating houses, at stated points on a long line of railroad through a wilderness, as in the case of the Pacific railroads, or at the end of a railroad on a barren, unsettled beach, as in the present case, not for the purpose of making money out of such business, but to furnish reasonable and necessary accommodations to its passengers and employees, would not be so plainly an act outside of the powers of a railroad company as to compel a court to sustain the defense of *ultra vires*, as against the other party to such a contract.

But even if the railroad company might be answerable for the rent of the premises, it is contended that the covenant to procure insurance was so far outside of the company's powers as not to be enforceable.

No one could deny that it would not be competent for a railroad company, without the authority of the legislature, to carry on an insurance business. But this covenant to keep the premises insured is correlative to the obligation of the lessors to rebuild in case the hotel should be destroyed by fire, and to the provision that, in such an event, the rents should cease until the hotel should be put in habitable condition and repair by the lessors. Such mutual covenants are quite usual in leases of this kind, and are merely incidental to the principal purpose of the contract. * * *

*Judgment affirmed.*⁴

Section 2.—To Acquire Its Own Shares or Those of Other Corporations.

CHICAGO, ETC., R. CO. v. PRESIDENT, ETC., OF MARSEILLES.

1877. 84 Ill. 643.¹

PER CURIAM: On considering the petition heretofore filed, we granted a rehearing to further consider the question, whether the railroad company had the power to contract for and purchase shares of stock of its own company. We have again fully examined the question, and, after considering the arguments and authorities bear-

⁴In *Malone v. Lancaster Gas etc. Co.* (1897) 182 Pa. St. 309, 37 Atl. 932, held that a corporation organized for the purpose of "manufacturing and supplying illuminating and heating gas" might not only deal in the gas itself, but could also incidentally deal in such patented appliances and conveniences as would induce new customers to use gas and old customers to use a larger quantity. Mitchell, J., said at p. 322: "In considering such questions, much weight must be allowed to the judgment of the parties most interested, the officers and stockholders of the corporation itself, and while they will not be permitted, as against the commonwealth or a dissenting stockholder, to go outside of their legitimate corporate business, yet where the act questioned is of a nature to be fairly considered incidental or auxiliary to such business, it will not be unlawful, because not within the literal terms of the corporate grant."

In *People v. Campbell* (1894) 144 N. Y. 166, 38 N. E. 990, held that a corporation organized for the manufacture and sale of gold and silverware was not authorized to purchase and sell goods manufactured by other parties. Andrews, Ch. J., said at p. 172: "The unexpressed and incidental powers possessed by a corporation are not limited to such as are absolutely or indispensably necessary to enable it to exercise the powers specifically granted. Whatever incidental powers are reasonably necessary to enable it to perform its corporate functions are implied from the powers affirmatively granted. (Comstock, J., *Curtis v. Leavitt*, 15 N. Y. 64.) But powers merely convenient or useful are not implied if they are not essential, having in view the nature and object of the incorporation."

See also *Thomas v. Railroad Co.* (1879) 101 U. S. 71, 25 L. ed. 950; *Brown v. Winnisimmet Co.* (1865) 11 Allen (Mass.) 326.—Eds.

¹The original opinion is reported in 84 Ill. 145.—Eds.

ing on the question, we will proceed to announce our conclusions thus reached.

The rule is familiar, and is not contested, that such bodies can only exercise such powers as may be conferred by the legislative body creating them, either in express terms or by necessary implication; and the implied powers are presumed to exist to enable such bodies to carry out the express powers granted, and to accomplish the purposes of their creation. Such being the rule, the question arises, whether this corporate body might make such a purchase, or is it outside of, and beyond the limit of its power?

Appellant has referred us to a number of cases in our own court, in which it has been held that such organizations have no power to release subscribers for their stock from paying therefor and from their subscriptions; that, when such subscriptions are intended to be fictitious or the subscribers are released from payment, it operates as a wrong, if not a fraud, on the other subscribers for stock in the same company. But here, the stock had been subscribed, paid for, and certificates thereof issued to, and they were owned and held by, the village at the time this contract was entered into and executed. So, the question is not, whether appellant may release the village from paying for and receiving shares subscribed for, but whether appellant has power to purchase shares of its own stock, paid for, issued to and held by the village.

In the case of *Taylor v. Miami Exportation Co.*, 6 Ohio (Hammond's R.) 83, it was held that a banking corporation might lawfully receive shares of its own stock from a solvent debtor in discharge of his indebtedness. The court went further, and held that, where a large number of shares had been issued to enable the holder to vote for certain persons for directors at an approaching election, and, after the holder had thus voted, the money paid for the shares was returned to him, and he restored the shares to the bank, as there was no loss sustained by the transaction, and the result of the election was not changed, and whilst the court condemned the transaction, it held that equity could afford no relief, as no one had been injured. It was also held in that case that, where the shares of that company were transferred to it in payment of such indebtedness, the corporation might hold and sell it as it did its other property.

In the case of *the City Bank of Columbus v. Bruce*, 17 N. Y. 507, it appeared that the board of directors passed a resolution that all stockholders indebted to the bank on stock note, by a specified day, might pay such debts to the bank in its shares of stock, at a named per cent., and that not far from half of the stock of the bank was thus surrendered; and the court held, there was no ground for questioning the validity of the transaction; that no rule of common law or any provision of the charter forbade it; and the Ohio case is referred to and approved by the court.

In the case of *William v. The Savage Manufacturing Company*, 3 Md. Ch. R. 452, it was held that banking corporations had the right

to take shares of their own stock in pledge or payment of indebtedness to the corporation, and to reissue the same. On the latter proposition *Ex parte Holmes*, 5 Cow. 426, is referred to by the court in its support.

In the case of *The State v. Smith*, 48 Vt. R. 266, it was held that where a railroad company had purchased 2,350 shares of the stock of the company, the stock did not merge, and the legality of the purchase seems to be recognized by the court. And in further support of the rule, see *Angell and Ames on Corp.*, sec. 280, where it is said it is one of the corporate powers that may be legally exercised.

If, then, as in cases above referred to, a bank may purchase and hold its own shares, no reason is perceived why a railroad corporation may not do the same thing, and the case of *The State v. Smith*, supra, was, the purchase of stock by a railroad company, and of shares of its own stock. These authorities, we think, fully recognize the power of the directors of a company, when not prohibited by their charter, to purchase shares of stock of their company. It falls within the scope of the powers of the directors to manage and control the affairs and property of the company for the best interests of the stockholders and when they have thus acted, we will presume, until the contrary is shown that the purchase was for legitimate and authorized purposes.

If it were shown that the purchase was made to promote the interests of the officers of the company alone, and not the stockholders generally, or if for the benefit of a portion of the stockholders and not all, or for the injury of all, or only a portion of them, or if operated to the injury of creditors, or would defeat the end for which the body was created, or if it was done for any other fraudulent purpose, then chancery could interfere. In such case, *Melvin v. The Lamar Ins. Co.*, 80 Ill. 446, and other cases in chancery referred to in appellant's brief, would apply, but the defense cannot be made at law. The case of *Belford Railroad Co. v. Bowser*, 48 Pa. St. R. 29, was in a court where there is no distinction between actions at law and suits in equity, and we presume the defense was allowed by the application of equitable principles, and the cases in the British courts which seem to bear on the question were in equity. Whatever may be the rights of stockholders, or creditors, if there are any, relief can only be had in equity and by a stockholder or other cestui que trust.

The judgment of the court below will, therefore, be affirmed.

*Judgment affirmed.*²

²*Dupee v. Boston Water Power Co.* (1873) 114 Mass. 37; *City Bank of Columbus v. Bruce* (1858) 17 N. Y. 507; *Moses v. Soule* (1909) 63 Misc. (N. Y.) 203, 118 N. Y. S. 410 (citing numerous authorities); *Porter v. Plymouth Gold Mining Co.* (1904) 29 Mont. 347, 74 Pac. 938; *Chapman v. Iron Clad Rheostat Co.* (1898) 62 N. J. L. 497, 41 Atl. 690 (statutory provisions); *Shoemaker v. Washburn Lumber Co.* (1897) 97 Wis. 585, 73 N. W. 333 ("provided the same is done in good faith, without intent to injure creditors thereof, and they are not injured thereby"); *In re Castle Braid Co.* (1906) 145 Fed. 224,

M'SHERRY, C. J., IN MARYLAND TRUST CO.
v. NATIONAL MECHANICS BANK.

1906. 102 Md. 608, 623-6, 63 Atl. 70.

THE case of *Trevor v. Whitworth*, 12 App. Cases, 409, is full upon the proposition that a corporation cannot traffic in its own stock or reduce its capital stock by purchasing its own shares. In the course of the learned judgment delivered by LORD HERSCHELL he referred to the case of *Hope v. International Financial Society*, 4 Ch. Div. 327, where it appeared that a company having 150,000 shares issued, passed a special resolution that the directors should have power to apply the company's assets to purchase from shareholders willing to sell any number of shares not exceeding 100,000, and that such shares should not be re-issued by the directors without the authority of a general meeting. "The Court of Appeals," said Lord Herschell, "affirming Vice-Chancellor Bacon held that this scheme was invalid." Lord Justice James in the *Hope* case said: "Either this is a purchase of shares in the sense of trafficking in shares, which is a purchase not authorized by the memorandum of association, or it is an extinguishment of the shares, and therefore a reduction of the capital of the company." And Lord Esher observed: "I agree with the Lord Justice that the dilemma is made perfect; for if you assume that there was to be a re-issue of these shares, the shares are not cancelled, they are existing shares, and the only way of getting rid of them again is to sell them. * * * If that therefore was the intention of the resolution, then it broke the rules, by enabling or forcing the company to enter upon a business which is not mentioned in the memorandum of association. But if it was not intended to re-issue the shares, then it seems to me to follow that the amount of capital represented by them was necessarily extinguished." And in *Guinness v. Land Corporation of Ireland*, 22 Ch. D. 349, Lord Justice Cotton, after referring to section 38 of the Companies Act, said: "From that it follows that whatever has been paid by a member cannot be returned to him. In my opinion, it also follows that what is described in the memorandum as the capital cannot be diverted from the objects of the society. It is, of course, liable to be spent or lost in carrying on the business of the company, but no part of it can be returned to a member so as to take away from the fund to which the creditors have a right to look as that out of which they are to be paid." In *Trevor v. Whitworth*, *supra*, a limited company was incorporated under the joint stock companies act with the objects (as stated in its memorandum) of acquiring and carrying on a manufacturing business. The company having gone into liquidation a

(*cf.* *Hamor v. Taylor-Rice Engineering Co.* (1897) 84 Fed. 392, distinguishing a purchase with funds representing capital from one with accumulated surplus), *Accord.*

As to creditors' rights, see *Clapp v. Peterson* (1882) 104 Ill. 26.—Eds.

former share holder made a claim against the company for the balance of the price of his shares sold by him to the company before the liquidation and not wholly paid for; and it was held by the House of Lords and Privy Council, reversing the decision of Court of Appeal, that such a company has no power under the Companies Act to purchase its own shares, that the purchase was therefore *ultra vires*, and that the claim must fail.

In Green's Brice's *Ultra Vires*, 95, it is said: "There is a great difference between dealing in the shares of other companies and its own. The former is ordinary business attended only with the usual risks of ordinary transactions, but the latter tends inevitably to breaches of their duty on the part of the directors, and to fraud and rigging the market on the part of the corporation itself. Consequently a corporation to possess such a power, must have it conferred by the plainest and most explicit language in its constituting instruments." In several states the power of a corporation to purchase its own shares has been denied, and it has been held that in the absence of express authority, a corporation, the amount of whose capital stock is fixed in its charter, has no power to purchase its own shares, either for the purpose of holding or selling or for the purpose of cancelling and retiring them. In addition to the cases already cited we may refer to the following as found in 7 Am. & Eng. Ency. L. (2nd ed.) 819; *San Luis Obispo Bank v. Wickersham*, 99 Cal. 655; *German Savings Bank v. Wulfekubler*, 19 Kan. 65; *St. Louis Carriage Manf. Co. v. Hilbert*, 24 Mo. App. 338; *Currier v. Lebanon State Co.*, 56 N. H. 262; *Morgan v. Lewis*, 46 Ohio St. 1. The reasons given for the doctrine, apart from any express or implied statutory prohibition, are, that the purchase of its own stock by a corporation is not only a fraud upon the creditors who deal with the corporation on the faith that the capital is paid up, and a fraud upon and violation of the contract with the stockholders who do not consent, but is also a violation of the charter. "The capital stock of a corporation," says Thompson, "being a trust fund for creditors, the general rule, in the absence of an enabling statute, is that a corporation cannot employ its funds in purchasing its own shares, thus distributing its capital among its shareholders to the manifest detriment of its creditors." 2 Thomp., section 2054. And as to the protection of the stockholders see 7 Am. & Eng. Ency. L., 819 notes, where it is said each stockholder has the right to insist that the capital shall remain and not be distributed to any other stockholder, and that to purchase shares and to pay for them out of the funds of the company would be a fraud upon the remaining stockholders.

From these cases (and others in addition might be cited) it seems perfectly manifest that a corporation by the purchase of its own shares, in the absence of legislative authority permitting that to be done, diminishes its capital to the extent of the shares so purchased, and this, too, although the purchase was intended to serve only a temporary purpose, save in the instance where the stock is bought

to secure the payment of an antecedent debt. *First Nat. Bank v. Nat. Exchange Bank*, 39 Md. 600. If such purchases effect a reduction of the stock, then, as that method of reducing the stock is not the method provided by the Code, it must of necessity be an unlawful method, and a contract entered into with a view of carrying out an unlawful method is a contract to do an unlawful thing, and consequently is an unlawful contract. Under such circumstances a plaintiff must look elsewhere than to a court of justice for such assistance as he may require. It was aptly remarked in *Re Dronfield Silk Stone Co.*, 17 Ch. D. 83, "It is inconsistent with the essential nature of a company that it should become a member of itself." And that is precisely what it does when it buys its own stock.

Aside from these direct adjudications it would seem to be clear as a necessary consequence from a corporation's want of power to release an unpaid subscription to its stock, that it was without authority to buy its own shares and thereby reduce the amount of its capital. "I can see," remarked the Master of Rolls, "no distinction in principle, between returning to a shareholder a part of the paid-up capital in exchange for his shares, and wiping out his liability for the uncalled-up sum payable thereon. Both methods involve a reduction of capital, which, as LORD WATSON pointed out in *Trevor v. Whitworth*, persons dealing with this company are entitled to rely upon as existing, either as paid up, or still to be called up, and such a reduction, therefor, can only hold good if sanctioned under the conditions prescribed." *Bellerby v. Rowland*, 2 Ch. (1902) 14. If a corporation be incompetent to release subscribers to its capital stock whose subscriptions have not been paid, it is equally without authority to expend the fund represented by the capital stock, to purchase shares held by a stockholder who has paid for them.*

* *Trevor v. Whitworth* (1887) 12 App. Cas. 409 (especially opinion of Lord Herschell); *German Sav. Bank v. Wulfekuhler* (1877) 19 Kan. 60; *State v. Oberlin etc. Loan Assn.* (1879) 35 Oh. St. 258; *Cartwright v. Dickinson* (1889) 88 Tenn. 476, 12 S. W. 1030, 17 Am. St. 910, 7 L. R. A. 706. *Accord.*

"It is true, however, that in most jurisdictions, where the right of a corporation to traffic in its own stock has been denied, an exception to the rule has been admitted to exist, whereby a corporation has been allowed to take its own stock in satisfaction of a debt due to it. This exception is supposed to rest on a necessity which arises in order to avoid loss; and was recognized in this state as early as *Taylor v. Miami Exporting Co.*, 6 Ohio 176." *McIlvaine, J.*, in *Coppin v. Greenless & Ransom Co.* (1882) 38 Oh. St. 275, at page 279, 43 Am. Rep. 425. See also *First National Bank v. National Exchange Bank* (1875) 92 U. S. 122, 23 L. ed. 679; *Morgan v. Lewis* (1888) 46 Oh. St. 1, 17 N. E. 558.—Eds.

IN RE ASIATIC BANKING CORPORATION.

1869. L. R. 4 Ch. App. Cas. 252.⁴

SIR C. J. SELWYN, L. J.—The memorandum of association constituting the *Royal Bank of India* declares its object to be to carry on the trade of bankers; and its power to do everything incidental to the business of banking is expressed in the most wide and unlimited terms. * * *

Now, with respect to the first question which has been argued, viz., as to the capacity of a trading corporation to accept shares in another trading corporation, it is sufficient for me to say that I entirely agree with the judgment of Lord Cairns in the case of *Barned's Banking Company*,⁵ viz., that there is not, either by the common or statute law, anything to prohibit one trading corporation from taking or accepting shares in another trading corporation. There may, of course, be circumstances which prohibit or render it improper for a company to do so, having regard to its own constitution as defined by its memorandum and articles; but excluding all these considerations, although in the statute of 1862 the words "person or persons" continually occur, still I think it must be taken to include corporations, and looking at the question as a mere abstract question, in my judgment there is nothing to prevent a corporation from being a shareholder in another trading corporation.⁶

FRANKLIN BANK v. COMMERCIAL BANK.

1881. 36 Ohio St. 350.⁷

ACTION in conversion against a corporation for refusal to transfer shares alleged to have been pledged to plaintiff corporation as security for a loan.

BOYNTON, J.—We are met at the threshold of the case with the

⁴ Only portion of the opinion is given.—Eds.

⁵ (1867) L. R. 3 Ch. App. Cas. 105. *Held*, a corporation might become a shareholder in another corporation, if so authorized by its memorandum and articles of association.—Eds.

⁶ *Booth v. Robinson* (1881) 55 Md. 419; *Robotham v. Prudential Ins. Co.* (1903) 64 N. J. Eq. 673, 53 Atl. 842, (statutory provision), *Accord*.

"It must be said at once, that where the purchase of stock in one corporation by another amounts to engaging in a business other than that authorized by its charter, such purchase is *ultra vires*, and this is so, not because the purchase is stock, but because the business is outside the scope of its charter. Whether the purchase of stock in one corporation by another is *ultra vires* or not, must depend upon the purpose for which the purchase was made, and whether such purchase was, under all the circumstances, a necessary or reasonable means of carrying out the object for which the corporation was created, or one which under the statute it might accomplish." *Mitchell, J.*, in *Hill v. Nisbet* (1884) 100 Ind. 341.—Eds.

⁷ Statement rewritten. Portion of opinion omitted.

inquiry, whether an action will lie in favor of the plaintiff against the defendant for refusing to transfer, on the books of the defendant, to the name of the plaintiff, the two hundred shares of the capital stock of the defendant, represented by the certificate issued to Foote, and by him pledged to the plaintiff as security for the loan obtained. Such refusal to so transfer said stock, and an alleged consequent conversion of the same by the defendant, constitute the gravamen of the plaintiff's action. The 12th section of the act under which the two corporations were organized and from which they derived their powers, expressly provided, that no banking company organized under its provisions should be the holder or purchaser of any portion of its capital stock or of the capital stock of any other incorporated company, unless such purchase should be necessary to prevent loss upon a debt previously contracted in good faith, on security which, at the time, was deemed adequate to insure the payment of such debt, independent of any lien upon such stock. 1 S. & C. 170, § 12. And by section 29 it was provided, that all the rights, privileges and franchises which the company derived from the act should be forfeited, if the directors of the company should knowingly violate, or permit any of the officers or agents of the company to violate, any of the provisions of the act. That the stock in the present case was pledged or received to secure a precedent loan is not claimed.

There would seem to be little doubt, either upon principle or authority, and independently of express statutory prohibition of the same, that one corporation cannot become the owner of any portion of the capital stock of another corporation, unless authority to become such is clearly conferred by statute. *Mutual Savings Bank &c. v. Meriden Agency*, 24 Conn. 159; *Franklin Company v. Lewiston Savings Bank*, 68 Me. 43; *Central Railroad Company v. Collins*, 40 Ga. 582; *Sumner v. Marcy*, 3 W. & M. 105. Were this not so, one corporation, by buying up the majority of the shares of the stock of another, could take the entire management of its business, however foreign such business might be to that which the corporation so purchasing said shares was created to carry on. A banking corporation could become the operator of a railroad, or carry on the business of manufacturing, and any other corporation could engage in banking by obtaining the control of the bank's stock. Nor would this result follow any the less certainly, if the shares of stock were received in pledge only, to secure the payment of a debt, provided the shares were transferred on the books of the company to the name of the pledgee. A person in whose name the stock of the corporation stands on the books of the corporation, is, as to the corporation, a stockholder, and has the right to vote upon the stock. *State ex rel. White v. Ferris*, 42 Conn. 560; *Exp. Willcocks*, 7 Cow. 402; *In re Barker*, 6 Wend. 509; *Hoppin v. Buffum*, 9 R. I. 513; *Field on Corp.*, § 69.

Hence, if the plaintiff appeared on the books of the defendant as the transferee or owner of the two hundred shares of stock represented by the certificate to Foote, it would have the right to vote upon the stock at all meetings of the stockholders of the defendant; and it would only be necessary for it to procure in pledge, as security for money loaned, a majority of the shares of the capital stock of the Commercial Bank, in order to obtain full control of its affairs, and take charge of its banking operations. This would not only be exercising powers granted to the plaintiff neither expressly nor by implication, but those which are clearly opposed to the manifest spirit and intent, if not to the language, of the statute. This court has uniformly adhered to the doctrine announced in *Straus v. Eagle Ins. Co.*, 5 Ohio St. 59, that corporations have such powers, and such only, as the act creating them confers; and are confined to the exercise of those expressly granted, and such incidental powers as are necessary to carry into effect those specifically conferred. *Bank of Buffalo v. Toledo F. & M. Ins. Co.*, 12 Ohio St. 601. This principle has recently been most emphatically asserted, both by the Supreme Court of the United States in *Thomas v. Railroad Co.*, 101 U. S. 71, and by the House of Lords in *Ashbury Railroad Carriage and Iron Co. v. Riche*, L. R. 7, H. L. 653. It was claimed in argument in both of these cases that a corporate body may do any act which is not either expressly or impliedly prohibited by its charter; although it was conceded, that a stockholder might enjoin the act where it was not authorized, either expressly or by implication, and that the state, by proper process and proceedings, might forfeit the charter. But it was held in the first case, that the powers of a corporation organized under a legislative enactment, are such only as the statute confers, and that the enumeration of them implies the exclusion of all others. And by the second case, that the contract sued on, being of a nature not included in the Memorandum of Association, was *ultra vires*, not only of the directors, but of the whole company, and which the whole body of shareholders was incapable of ratifying.

Notwithstanding the rule thus prevailing, the act under which both the plaintiff and defendant were organized, did not leave the right or power of the plaintiff to acquire the title to shares of stock in another corporation, to be determined alone upon the principle of construction which the rule above stated adopted. The right to deal in shares of stock in other corporations is not only not found among the enumerated powers which the act confers upon banks organized under its provisions, but the power, in language of the most undoubted import, is denied, and its exercise expressly prohibited. It therefore follows that the refusal of the defendant to permit the transfer upon its books to the plaintiff of the two hundred shares of its stock, violated no right of the plaintiff, and consequent-

ly created no liability on the part of the defendant. (Such refusal did not amount to a conversion of the stock.

Judgment affirmed.^a

* *Commercial Fire Ins. Co. v. Board of Revenue* (1891) 99 Ala. 1, 14 So. 490; *Byrne v. Schuyler etc. Mfg. Co.* (1895) 65 Conn. 336, 31 Atl. 833; *People v. Chicago Gas Trust Co.* (1889) 130 Ill. 268, 22 N. E. 798 (corporation organized to manufacture and sell gas not authorized to purchase and hold stock in similar corporations); *Franklin Co. v. Lewiston Savings Bank* (1877) 68 Me. 43, 28 Am. Rep. 9; *Woodberry v. McClurg* (1901) 78 Miss. 831, 29 So. 514 ("no corporation shall directly or indirectly purchase or own the capital stock, or any part thereof, of any other corporation, and that, too, without any question of competition between them"); *Holmes etc. Mfg. Co. v. Holmes etc. Metal Co.* (1891) 127 N. Y. 252, 27 N. E. 831 (citing numerous authorities); *Easun v. Buckeye Brewing Co.* (1892) 51 Fed. 156, *Accord.* But see *Davis v. United States etc. Light Co.* (1893) 77 Md. 35, 25 Atl. 982. See also *California National Bank v. Kennedy* (1897) 167 U. S. 362, 42 L. ed. 198, 17 Sup. Ct. 831. See note by C. G. Little, 4 Ill. Law Rev. 581-3.

"Certain classes of corporations, such as religious and charitable corporations, and corporations for literary purposes, may rightfully invest their moneys in the stock of other corporations. The power, if not expressly mentioned in their charters, is necessarily implied, for the preservation of the funds with which such institutions are endowed, and to render their funds productive. So an insurance company or savings bank may rightfully invest its capital or deposits in the stocks of railroad companies, banks, manufacturing companies, and similar corporations. The power is necessary to enable them to engage in the business for which they are organized, and hence is implied, if not expressly granted, in their charters. Such investments are in the line of their business. On the other hand, a manufacturing or railroad corporation is incorporated to do the business of manufacturing, or transporting passengers and merchandise. Investing their funds in that of other corporations is not in the line of their business. Under extraordinary circumstances it may become necessary for a national bank, or a manufacturing corporation, or a railroad corporation, to acquire stock in another corporation, as in satisfaction of a valid debt, or by way of security, but with a view to its subsequent sale or conversion into money so as to make good or redeem an anticipated loss. *Bank v. Bank*, 92 U. S. 128; *Fleckner v. Bank*, 8 Wheat. 351." *Smith, J., in Pearson v. Concord R.* (1883) 62 N. H. 537.—Eds.

Section 3.—To Enter Into a Copartnership.

MALLORY v. HANAUR OIL WORKS.

1888. 86 Tenn. 598, 8 S. W. 396.¹

LURTON, J.—This is an action of unlawful detainer, brought by the Hanaur Oil Works, a corporation created under the General Incorporation Act of 1875, and engaged in the manufacture of cotton seed oil at Memphis, Tenn.

The facts which raise the question to be determined are these: In July, 1884, a contract was entered into by and between four corporations engaged in manufacturing cotton seed oil at Memphis for

¹ Portion of opinion omitted.—Eds.

the formation of what is designated in the agreement as a "combination syndicate" and "partnership." The contracting mills agreed to select a committee, composed of representatives from each corporation, and to turn over to this committee the properties and machinery of each mill, to be managed and operated by this committee, through officers, agents and employes selected by them, for the common benefit, the profits and losses of such operations to be shared in proportions agreed upon. This arrangement was to last one year, but, with consent of all, might be renewed for two additional years, and, as appears, was at end of first year renewed for two other years, terminating August 1, 1887.

The facts clearly established that the possession of several mills was turned over to this executive committee, and they were operated by these managers thenceforward under the name of the "Independent Cotton Seed Association." There was a provision in the contract by which other mills were to be admitted by consent, and a fifth corporation was in fact subsequently admitted. The Hanaur Oil Works was one of these contracting corporations, the contract being authorized by both shareholders and directors. In July, 1886, the business of the second year having been about concluded, the board of directors of the Hanaur Oil Works passed a resolution declaring this contract void, as being an agreement *ultra vires*, and their president was instructed to take possession of their mill. There is some proof tending to show that, upon demand of the president of the defendant in error, the general superintendent of the "Independent Cotton Seed Association" surrendered possession of the Hanaur mill to him, and agreed to hold for him, and that he afterward repudiated this agreement by surrendering possession to Mr. Mallory, one of the executive committee, who thereupon locked up the mill, and gave instructions to a watchman in the employ of the committee not to admit the Hanaur officers.

In the view we take of the case it is not material to determine the legal effect of the evidence upon this question, as to what passed between Mr. Camp, the superintendent, and Mr. Cochran, the president. The fact is, that at the time the writ of unlawful detainer was sued out the mill of the Hanaur Company was in the exclusive possession of the officers of the "Independent Cotton Seed Association," and the officers of the Hanaur company were excluded therefrom. There was a judgment in favor of the Hanaur Oil Works, and from this an appeal has been prosecuted.

The argument here has largely turned upon the correctness of the charge of the circuit judge, who distinctly instructed the jury that the contract between the Hanaur company and the other four corporations was a contract for a partnership between corporations, and that under the charter of the Hanaur Oil Works it had no power to make such a contract, and that it was therefore void, and that it had a right to recover possession of its property, it being withheld solely under and by virtue of an agreement *ultra vires*. * * *

A careful examination of this agreement discloses every material element to a contract of partnership. The absolute ownership of the corporate property, the mill's machinery, etc., is not conveyed to the partnership, nor is this necessary. The beneficial use of all such property is surrendered to the common purpose. The provisions for the complete possession, control, and use of the properties of the several corporations by the partnership or syndicate is perfect. Nothing is left of the several corporations, but the right to receive a share of the profits and participate in the management and control of the consolidated interests as one of the new association. The contract is, both technically and in its essential character, a partnership in so far as it is possible for corporations to form such an association.

It is, however, argued by the learned counsel for appellants that if it be a partnership that it does not therefore follow that it is ultra vires; that such a contract, not being prohibited by law or the charter of the defendant in error, or against public policy, is not void, even if in excess of power expressly conferred; that the business proposed by the contract, being within the purposes of the charter, is therefor within the implied powers of the corporation, and not ultra vires. In other words, "that the question is not whether the corporation had, by virtue of the act of incorporation, authority to make the contract, but whether they are by those statutes *forbidden* to do it." In this doctrine we do not concur. There is, however, respectable authority for the position. A corporation, being an artificial creation, is the very thing it is made by the statute which brings it into being, and nothing more. The extent of its powers are those enumerated in its charter, or implied by fair and natural construction of powers expressly conferred.

The charter is the measure of its powers, and the enumeration thereof implies the exclusion of all others. We are not to look to the charter to see whether the thing done be prohibited, but whether there is authority to do it. These principles we understand to have the support of the great weight of authority in this country, and to have the sanction of the Supreme Court of the United States. *Thomas v. Railroad Company*, 101 U. S. 71.

This view of the law has been the one entertained by this court, and clearly and distinctly enforced in an opinion by the present Chief Justice in the case of *Elevator Company v. Memphis and Charleston Railroad Company*, 1 Pick. 703. The power to enter into a partnership is not expressly or impliedly conferred by our act of 1875, under which the Hanaur Oil Works is incorporated. Neither is such authority within the implied powers of corporations. A partnership and a corporation are incongruous. Such a contract is wholly inconsistent with the scope and tenor of the powers expressly conferred and the duties expressly enjoined upon a corporation, whether it be a strictly business and private corporation or one owing duties to the public, such as a common carrier. In a partner-

ship each member binds the firm when acting within the scope of the business. A corporation must act through its directors or authorized agents, and no individual member can, as such member, bind the corporation.

Now, if a corporation be a member of a partnership, it may be bound by any other member of the association, and in so doing he would act not as an officer or agent of the corporation, and by virtue of authority received from it, but as a principal in an association in which all are equal, and each capable of binding the society by his acts. The whole policy of the law creating and regulating corporations, looks to the exclusive management of the affairs of each corporation by the officers provided for or authorized by its charter. This management must be separate and exclusive, and any arrangement by which the control of the affairs of the corporation should be taken from its stockholders and the authorized officers and agents of the corporation, would be hostile to the policy of our general incorporation acts. The decided weight of authority is that a corporation has not the power to enter a partnership, either with other corporations or individuals. Says Mr. Morawetz: "It seems clear that corporations are not impliedly authorized to enter into partnership with other corporations or with individuals. The existence of a partnership not only would interfere with the management of the corporation by its regularly appointed officers, but would impair the authority of the shareholders themselves, and involve the company in new responsibilities through agents over whom it had no control." 1 Morawetz on Corporations, § 421; Whittenton Mills v. Upton, 10 Gray, 582 (S. C., 71 Am. Dec. 681); Angel & Ames on Corporations, § 272.

It is unnecessary to consider this contract as constituting a mere traffic arrangement; for the conclusion already announced that it was an effort to form a partnership, determines that in its scope and effect it sought to accomplish much more than would be understood by the phrase "traffic arrangement." * * *

That the defendant in error has submitted to a void contract, by which it has been deprived of the use of its property for two years, furnishes no sound reason why it shall submit for three years. To hold that it did, would be to apply the doctrine of part performance in a way to perfect and legalize illegal contracts which were partly performed.

We have not deemed it necessary to consider the question of the legality of such a combination of corporations as one tending to create a monopoly, for the ground upon which we place the case needs no additional prop. The question of the validity of such an arrangement is a very grave one, but need not now be considered. * * *

The result is, that we hold that there was no error in the charge of the Circuit Judge, or his refusal to charge, and the judgment must be affirmed, with costs.²

² Bishop v. American Preservers Co. (1895) 157 Ill. 284, 41 N. E. 765; Whit-

WILSON v. CARTER OIL CO.

1899. 46 W. Va. 469, 33 S. E. 249.

ENGLISH, J.—This was an action of trespass on the case, in assumpsit, instituted in the circuit court of Tyler County by L. C. Wilson and the Devonian Oil Company, a corporation, partners doing business under the firm name of L. C. Wilson & Co., against the Carter Oil Company, a corporation under the laws of the state of West Virginia, for work and labor performed and material furnished to the defendant amounting to five hundred and twelve dollars. The defendant tendered a special plea, averring that the plaintiff ought not to maintain its action against the defendant for the reason that the Devonian Oil Company, one of the plaintiffs, and a member of the partnership which brings this suit is a corporation of the state of Pennsylvania, and, under the laws of that state and its charters, it had no power to enter into this or any other partnership, and therefore the plaintiff ought not to maintain this suit; and of this the defendant put itself upon the country. The defendant further pleaded non-assumpsit and payment, with leave to file special matter in evidence. The plaintiffs demurred to the defendant's special plea, in which demurrer the defendant joined. The court overruled the demurrer, sustained the defendant's plea, and found for the defendant, and the plaintiffs obtained this writ of error.

The sole question, then, presented for consideration by this record, is whether the circuit court erred in sustaining said plea and dismissing plaintiff's action. As to the question whether a corporation can form a partnership with an individual, the authorities are conflicting. It is believed that the weight of authority is to the effect that a corporation cannot form a partnership with an individual. In 7 Am. & Eng. Enc. Law (2d Ed.) 794, the law is stated thus: "A corporation has no power to form a partnership with an individual, unless authorized to do so by its charter." And in Morawetz on Corporations (section 421) thus: "It seems clear that corporations are not impliedly authorized to enter into partnership with other companies or individuals." And Beach Priv. Corp., section 842, says: "One firm may be a partner with another firm, and there is no general principle of law which prevents a corporation from being a partner with another corporation or with ordinary individuals, except the principle that a corporation cannot lawfully employ its funds for purposes not authorized by its constitution. Having

tenton Mills v. Upton (1858) 10 Gray (Mass.) 582; White Star Line v. Star Line (1905) 141 Mich. 604, 105 N. W. 135; People v. North River Sugar Ref. Co. (1890) 121 N. Y. 582, 24 N. E. 834, *semble* ("It has helped to create an anomalous trust which is in substance and effect, a partnership of twenty different corporations. * * * It is a violation of law for corporations to enter into a partnership."); Fechteler v. Palm Bros. (1904) 133 Fed. 462, 66 C. C. A. 336, *Accord*. But *cf.* Ontario Salt Co. v. Merchants Salt Co. (1871) 18 Grant's Ontario Ch. 540.—Eds.

regard, however, to this principle, it may be considered as *prima facie ultra vires* for an incorporated company to enter into a partnership with other persons." Also, in 7 Am. & Eng. Enc. Law (New Ed.) 794, it is said: "By the decided weight of authority, a corporation has no power to enter into an ordinary contract of partnership with another corporation, or an individual or individuals, unless such power is expressly conferred upon it by its charter." The question presented by the record in this case is not limited to the mere inquiry whether a corporation can form a partnership with an individual, but whether the defendant's plea constitutes a good defense to this action; in other words, if the plaintiffs were not partners in the strict sense of the word, can we say their recovery in this action is necessarily defeated? In *Courson v. Parker*, 39 W. Va. 521 (20 S. E. 583), this court held that: "At common law, partners cannot be sued otherwise than in their individual names, and the allegation of a partnership name is merely for the purpose of identification and description, is immaterial, and need not be proven; and hence the unnecessary use of it may be regarded as mere surplusage." The same rule would apply to plaintiffs as defendants, and in the case at bar the portion of the declaration describing the plaintiffs as partners may be treated as surplusage.

We find the law stated in a note on page 424, *Green's Brice Ultra Vires*, as follows: "There is nothing, however, to prevent a corporation from becoming interested in a transaction jointly with another corporation or with an individual so as to be joint plaintiffs or defendants in an action." In *New York & S. Canal Co. v. Fulton Bank*, 7 Wend. 412, it is held that "two incorporated companies may unite in an action of assumpsit to recover a sum of money deposited in bank in their joint names." Also, in *Bank v. Ogden*, 29 Ill. 248, it is held that, "as a general rule, corporations are not capable of forming a partnership, but they may make joint contracts by which both bodies may become liable." What is true of two corporations as stated in this decision is also true of one corporation and an individual, and if, acting thus, they are capable of rendering themselves liable, other parties may by contract become liable to them. So, in *2 Beach Priv. Corp.*, p. 1317, section 842, it is said: "The results of partnership arrangements between corporations and individuals have been subjected to the rules governing partnerships, and their contracts enforced, even when the agreement has not been upheld. Accordingly, where a corporation and an individual have assumed to enter into partnership and jointly transact business together, they may, by reason of their joint interest, recover upon obligations made to them in their partnership name, irrespective of their partnership rights and duties as between themselves, or the capacity of the association to execute the powers incident to a partnership," citing *Cleveland Paper Co. v. Courier Co.*, 67 Mich. 152 (34 N. W. 556); *Manufacturing Co. v. Sears*, 45 N. Y. 799; *Legget v. Hyde*, 58 N. Y. 272; *Raft Co. v. Roach*, 97 N. Y. 378. A case di-

rectly in point is that of *French v. Donahue*, 29 Minn. 111 (12 N. W. 354), in which the court holds that "where an association or corporation and another have assumed to enter into partnership, and jointly transacted business together, they may recover by reason of their joint interest, upon obligations made to them in their partnership name, irrespective of their partnership rights and duties as between themselves, or the power of such association to execute the powers incident to a partnership." When the declaration in the case under consideration is relieved of its surplusage, it only claims that the defendant is indebted to L. C. Wilson and the Devonian Oil Company in the sum of five hundred and twelve dollars for work and labor performed for, and for goods and chattels sold and delivered to, the defendant, for which the defendant promises to pay them; and, after getting the benefit of the labor and receiving the goods and chattels, the law will not allow the defendants, by special plea, to avoid its liability by averring that one of the parties with whom it contracted was a corporation, and incapable of forming a partnership. Whether the plaintiffs were partners or not, the liability was incurred by the defendant assuming the payment of the account to the plaintiffs jointly; and my conclusion is that the court erred in overruling the plaintiffs' objection to said plea, and allowing the same to be filed, and in dismissing the plaintiffs' action. The judgment complained of is therefore reversed and the cause remanded. *Reversed.*³

Section 4.—To Alienate All Its Property.

PEOPLE EX REL. BARNEY v. WHALEN.⁴

1907. 119 App. Div. (N. Y.) 749, 104 N. Y. S. 555.

APPEAL by the relator, Charles T. Barney, from an order of the Supreme Court, made at the Albany Special Term and entered in the

³ See also *Breinig v. Sparrow* (1907) 39 Ind. App. 455, 80 N. E. 37; *Kelly v. Biddle* (1901) 180 Mass. 147, 61 N. E. 821; *Cleveland Paper Co. v. Courier Co.* (1887) 67 Mich. 152, 34 N. W. 556 ("A corporation may, in furtherance of the object of its creation, contract with an individual, though the effect of the contract may be to impose upon the company the liability of a partner."); *French v. Donahue* (1882) 29 Minn. 111, 12 N. W. 354; *Catskill Bank v. Gray* (1851) 14 Barb. (N. Y.) 471; *Swift v. Pacific Mail Steamship Co.* (1887) 106 N. Y. 206, 12 N. E. 583 (joint contracts for transportation between corporations with connecting facilities); *Hackett v. Multnomah R. Co.* (1885) 12 Ore. 124, 6 Pac. 659 (joint ownership of ferry); *Boyd v. American Carbon Black Co.* (1897) 182 Pa. St. 206, 37 Atl. 937 (accounting); *Allen v. Woonsocket Co.* (1876) 11 R. I. 288 (partnership terminable at will); *Huguenot Mills v. Jempson* (1903) 68 S. Car. 363, 47 S. E. 687; *Wallerstein v. Ervin* (1901) 112 Fed. 124 (corporation not allowed to repudiate its copartnership agreement with firm and to claim as creditor in competition with firm's general creditors); *Roedde v. News-Advertiser Pub. Co.* (1894) 4 British Columbia 7.

⁴ "There is no rule of law that will preclude a corporation from entering

office of the clerk of the county of Albany on the 23rd day of February, 1907, denying the relator's motion for a peremptory writ of mandamus to compel the defendant to file a certificate of incorporation.

CHESTER, J.:

The order appealed from denies the application of the relator for a peremptory writ of mandamus requiring the respondent to file in his office a certificate of incorporation. The secretary refused to file the certificate because there was contained therein the following clause:

"The directors may, with the consent of the holders of two-thirds of the capital stock, issued and outstanding, sell, assign, transfer or otherwise dispose of, the whole of the property of the corporation, not including franchises, to any person or corporation, domestic or foreign."

The respondent, as Secretary of State, was not required to file a certificate of incorporation if it contained provisions unauthorized by law. (*People ex rel Blossom v. Nelson*, 46 N. Y. 447.) Section 2 of the Business Corporations Law (Laws of 1892, Chap. 691, as amd. by Laws of 1895, Chap. 671; Laws of 1896, Chaps. 369, 460; Laws of 1901, chap. 520; Laws of 1903, chap. 525, and Laws of 1904, chap. 446), under which it was proposed to file the certificate in question, prescribes what a certificate of incorporation thereunder must contain. The clause objected to is clearly outside of any of the requirements there specified. That section also contains the following provision: "The certificate may contain any other provision for the regulation of the business and conduct of the affairs of the corporation and any limitation upon its powers and upon the powers of its directors and stockholders which does not exempt them from any obligation or from the performance of any duty imposed by law."

Substantially the same provision is also included in section 10 of the General Corporation Law (Laws of 1892, chap. 687, as amd. by Laws of 1895, chap. 672). That section also provides that "No corporation shall possess or exercise any corporate powers not given by law or not necessary to the exercise of the powers so given."

If, therefore, the clause in question, which the respondent objected to, was one which purported to give the proposed corporation powers, or the right to exercise powers not given by law, he was justified in withholding his assent to such filing. That clause is not one regulating the business or relating to the conduct of the affairs of the corporation but is rather one for the purpose of ending or closing up its business or affairs. It is not one limiting its powers or those of its directors and stockholders but is one intended to enlarge such pow-

into a contract with an individual, which will have the effect to carry out directly or indirectly the object of its incorporation, and to provide in that agreement that the gains or losses of the venture shall be borne equally by both parties."—*Harrison, J., in Bates v. Coronado Beach Co.* (1895) 109 Cal. 160, 41 Pac. 855.

ers. It assumes to give the directors of the corporation, with the consent of the holders of two-thirds of the outstanding capital stock issued, the right to dispose of the whole of the property of the corporation, except its franchises, to any person or corporation, domestic or foreign.

The statutory power to sell the property of a corporation is found in section 33 of the Stock Corporation Law (Laws of 1892, chap. 688, added by Laws of 1893, chap. 638, and amd. by Laws of 1901, chap. 130). That section gives a domestic stock corporation, except a railroad corporation, and except as otherwise provided by law, with the consent of two-thirds of its stockholders, the right to sell and convey its property, rights, privileges and franchises, or any interest therein, to a domestic corporation engaged in a business of the same general character; and it also provides that a domestic corporation, the principal business of which is carried on in, and the principal tangible property of which is located within, a State adjoining the State of New York, may, with the consent of the holders of ninety-five percentum of its capital stock, sell and convey its property situate without the State, not including its franchise, to a corporation organized under the laws of such adjoining State.

The clause which the respondent objects to authorizes the directors to dispose of the whole of the property of the proposed corporation, except its franchises, to a domestic or to a foreign corporation, on the consent of two-thirds of the capital stock issued and outstanding, and, therefore, it is an attempt to procure the right to exercise powers in this respect not conferred by the statute which, as we have seen, prohibits a domestic corporation from so transferring its property to a domestic corporation unless it is engaged in a business of the same general character, and from transferring its whole property to a foreign corporation, except where the business of such corporation is carried on in an adjoining State, and even then such transfer can be made, under the statute, only upon the consent of ninety-five percentum of its stockholders, instead of two-thirds thereof.

The argument of the learned counsel for the appellant that corporations organized for private purposes and owing no duty of a public nature have always possessed and still possess a common-law right to convey their entire property to an individual or corporation upon the unanimous consent of the stockholders, may be conceded, yet that argument has no force as applied to the situation here. That power, if it exists, may be exercised by a corporation duly organized, not by virtue of anything stated in its certificate of incorporation, but by virtue of its corporate existence. The further argument that the insertion of a provision in the certificate of incorporation authorizing the corporation to dispose of its entire property, except franchises, to a foreign corporation upon the consent of a less percentage of the capital stock than the whole, is effective as the unanimous and irrevocable consent of all stockholders, given

in advance, to such a disposition, does not appeal to us as sound. A subscriber to the capital stock of a corporation is undoubtedly bound by such provisions of the certificate of incorporation as are lawfully inserted therein, but as the provision here is not one required by the statute it would not be effective to bind them except by virtue of some lawful agreement on their part to be bound thereby. More than this, we think the provisions of section 33 of the Stock Corporation Law above referred to stand in the way of permitting the directors of the proposed corporation to dispose of its entire property as above stated to a foreign corporation upon the consent of two-thirds only of its stockholders, because that section requires the consent of ninety-five per centum thereof for such disposition.

The order should be affirmed, with costs.
All concurred.¹

TREADWELL v. SALISBURY MFG. CO.

1856. 7 Gray (73 Mass.) 393.²

BIGELOW, J. * * *

The views which we have taken dispose of the whole case. It is therefore unnecessary to go at large into a consideration of the other branch of the cause, which was fully and elaborately discussed at the bar. But we entertain no doubt of the right of a corporation, established solely for trading and manufacturing purposes, by a vote of the majority of their stockholders, to wind up their affairs and close their business, if in the exercise of a sound discretion they deem it expedient so to do. At common law, the right of corporations, acting by a majority of their stockholders, to sell their property is absolute and is not limited as to objects, circumstances or quantity. Angell & Ames on Corp. § 127 & seq. 2 Kent Com. (6th ed.) 280. Mayor

¹ Affd. short, (1907) 189 N. Y. 560, 82 N. E. 1131.

A corporation on a solvent, going basis has no power to transfer all its property, thus effecting a practical dissolution, without the unanimous consent of its stockholders. Abbot v. American Hard Rubber Co. (1861) 33 Barb. (N. Y.) 578; Holmes etc. Mfg. Co. v. Holmes etc. Metal Co. (1891) 127 N. Y. 252, 27 N. E. 831; People v. Ballard (1892) 134 N. Y. 269, 32 N. E. 54; Elyea v. Lehigh Salt Mining Co. (1901) 169 N. Y. 29, 61 N. E. 992 ("it was competent, with the consent of its stockholders, for the corporation to sell its properties and to retire from the conduct of its business"); Schwab v. Potter Co. (1909) 194 N. Y. 409; 87 N. E. 670; Easun v. Buckeye Brewing Co. (1892) 51 Fed. 156. But see Cohen v. Big Stone Co. (1910) 111 Va. 486, 69 S. E. 359; Tanner v. Lindell R. Co. (1904) 180 Mo. 1, 79 S. W. 155.

In Harding v. American Glucose Co. (1899) 182 Ill. 551, 55 N. E. 577, held that where a corporation is "a solvent and going concern, and doing and able to continue to do a profitable business," the sale to another corporation of its entire property may be prevented by the protest of one dissenting shareholder.—Eds.

² Only portion of the opinion is given.—Eds.

&c. of *Colchester v. Lowton*, 1 Ves. & B. 226, 240, 244. Binney's Case, 2 Bland, 142. To this general rule there are many exceptions, arising from the nature of particular corporations, the purposes for which they were created, and the duties and liabilities imposed on them by their charters. Corporations established for objects quasi public, such as railway, canal and turnpike corporations, to which the right of eminent domain and other large privileges are granted in order to enable them to accommodate the public, may fall within the exception; as also charitable and religious bodies, in the administration of whose affairs the community or some portion of it has an interest to see that their corporate duties are properly discharged. Such corporations may perhaps be restrained from alienating their property, and compelled to appropriate it to specific uses, by mandamus or other proper process. But it is not so with corporations of a private character, established solely for trading and manufacturing purposes. (Neither the public nor the legislature have any direct interest in their business or its management.) These are committed solely to the stockholders, who have a pecuniary stake in the proper conduct of their affairs. By accepting a charter, they do not undertake to carry on the business for which they are incorporated, indefinitely, and without any regard to the condition of their corporate property. Public policy does not require them to go on at a loss. (On the contrary, it would seem very clearly for the public welfare, as well as for the interest of the stockholders, that they should cease to transact business as soon as, in the exercise of a sound judgment, it is found that it cannot be prudently continued.)

If this be not so, we do not see that any limit could be put to the business of a trading corporation, short of the entire loss or destruction of the corporate property. The stockholders could be compelled to carry it on until it came to actual insolvency. Such a doctrine is without any support in reason or authority. The case of *Ward v. Society of Attorneys*, 1 Collyer, 370, cited by the plaintiffs, does not support it. They were not a trading corporation; nor were their affairs in an embarrassed condition. It was the case of the majority of a corporation, attempting to surrender the old charter, and to pervert the corporate funds to a different purpose, by passing them over to a new association. Besides, the questions raised in the case were not finally determined by the vice chancellor. They were only considered so far as it was necessary to decide the question of granting an injunction preliminary to the hearing.

Upon the facts found in the case before us, we see no reason to doubt that the vote of the majority of the stockholders, for the sale of the corporate property, and the closing of the business of the corporation, was justified by the condition of their affairs. Without available capital, and without the means of procuring it, the further prosecution of their business would be unprofitable, if not impracticable. Under these circumstances it was in furtherance of the purposes of the corporation, to pay their debts, close their affairs and

settle with their stockholders on terms most advantageous to them. *Sargent v. Webster*, 13 Met. 504.

Nor can we see anything in the proposed sale to a new corporation, and the receipt of their stock in payment, which makes the transaction illegal. It is not a sale by a trustee to himself, for his own benefit; but it is a sale to another corporation for the benefit and with the consent of the cestuis que trust, the old stockholders. The new stock is taken in lieu of money, to be distributed among those stockholders who are willing to receive it, or to be converted into money by those who do not desire to retain it. (Being done fairly and not collusively, as a mode of payment for the property of the corporation, that transaction is not open to valid objection by a minority of the stockholders. *Hodges v. New England Screw Co.*, 1 R. I. 347.

It was urged by the plaintiffs that the common law right of a corporation to sell their property and close their business, had been taken away by St. 1852, c. 55. But we do not think that such is its true interpretation. It is not restrictive in its terms, but only permissive. It was intended to provide a mode in which the charter of a corporation might be dissolved without a resort to the legislature. But it did not take away the right of a corporation to proceed in the sale of their property preparatory to a surrender of their charter, which is all that the defendants undertook to do.

*Bill dismissed.**

* A corporation in failing circumstances may by majority vote of its shareholders alienate all its assets for the purpose of winding up its business and preventing further loss. *Bartholomew v. Derby Rubber Co.* (1897) 69 Conn. 521, 38 Atl. 45; *Price v. Holcomb* (1893) 89 Iowa 123, 56 N. W. 407; *Rogers v. Pell* (1898) 154 N. Y. 518, 49 N. E. 75 (assignment for benefit of creditors); *Werle v. Northwestern Flint & Sandpaper Co.* (1905) 125 Wis. 534, 104 N. W. 743.

In *Price v. Holcomb*, *supra*, Given, J., said: "If the majority decide arbitrarily, and without just cause, to sell the property of the corporation to the prejudice of the minority, and thereby compel the winding up of the business of the corporation, it is a fraud upon the minority, and courts of equity will interfere. If, however, just cause exists for selling the property, as when the corporation is insolvent, and the sale is necessary to pay debts, or where, from any cause, the business is a failure and an unprofitable one, and the best interests of all require it, the majority have clearly power to order the sale, and in such case their acts are not ultra vires. * * * It would be a harsh rule that would permit one stockholder to hold the others to their investment when just cause existed for closing the business of the corporation." See also *Hayden v. Official Hotel Red-Book etc. Co.* (1890) 42 Fed. 875.—Eds.

NOTE ON IMPLIED POWERS.

As pointed out in the principal cases, the determination of the implied powers of a corporation involves what is called a mixed question of law and fact that is, a question of fact to be determined by the court in accordance with certain general rules of interpretation and construction. One of these rules requires the court to consider (a) the character of the corporation, its objects and purposes, and (b) the means and methods which at any given time, according to approved usage or custom, are employed to accomplish these objects and purposes.

For the purpose of determining the implied powers, private corporations

may be divided, broadly speaking, into four classes, (a) ordinary manufacturing, mining or trading corporations, (b) moneyed corporations as defined in the N. Y. statute (General Corp. Law, sec. 3, subd. 4), namely, those subject to the banking or insurance law, (c) public-service corporations, such as railway companies, gas, electric light and power companies, and the like, (d) religious, charitable, educational, etc., corporations, such as churches, private hospitals, colleges, universities, and the like.

"The purposes of the defendant's (Commonwealth Trust Co.) organization are very material in determining the question as to its authority to make the alleged agreement. Where a corporation is organized for business or trading purposes and the only persons interested therein other than its business creditors are its stockholders and their only interest therein is to secure dividends upon their investment, the question of *ultra vires* is of comparatively small importance except in behalf of the people of the state in their public capacity, and the courts treat the question as it relates to such a corporation very differently than they do in the case of a banking corporation. (Hess v. Sloane, 66 App. Div. 522; affd. on opinion below, 173 N. Y. 616.) A banking corporation occupies a different relation to the public in that it invites individuals to submit to it the possession and care of their money and property. All banking institutions occupy a fiduciary position. * * * The courts, in considering the effect of *ultra vires* acts, have always recognized the distinction between business and trading corporations and corporations whose purposes are largely fiduciary." *Gause v. Commonwealth Trust Co.* (1909) 196 N. Y. 134, at pages 153-4, 89 N. E. 476.

In *Colman v. Eastern Counties R. Co.* (1846) 10 Beavan 1, Lord Langdale in considering the power of railway companies to encourage and finance subsidiary undertakings for the purpose of increasing traffic upon the lines, said: "It has been stated, that these things, to a small extent, have frequently been done since the establishment of railways; but unless the acts so done can be proved to be in conformity with the powers given by the special acts of parliament, under which those acts are done, they furnish no authority whatever. To suppose that the acquiescence of railway shareholders, for the last fifteen years, in any transaction conducted by a railway company, is any evidence whatever of their having a lawful right to enter into it, is, I think, wholly to forget the sort of frenzy which, during that period, the country has been in, * * * the acquiescence of the shareholders in such transactions, affords no ground whatever for the presumption of their legality. I am far from saying, that that which is here proposed to be done might not be profitable to this company, or that it might not be a public advantage. I am far from expressing an opinion that the establishment of a steam-packet at *Harwich*, communicating with this railway, might be not only of public, but of national, importance, or that it might not be proper to give this company authority to do that which they are now attempting to do, as it seems to me, without authority: I mean to express no opinion as to this." (pages 15-16). The learned judge continued the injunction restraining the directors of the railway company from financing a projected steamship company to operate between its English terminus and the northern ports of Europe.

At common law a corporation has in general an implied power

(1) to use a seal, and according to the American doctrine to make contracts without the use of a seal. *Bank of Columbia v. Patterson's Admr.* (1813) 7 Cranch (U. S.) 299, 3 L. ed. 351; *Bank of United States v. Dandridge* (1827) 12 Wheat. (U. S.) 64, 6 L. ed. 552; *Gottfried v. Miller* (1881) 104 U. S. 521, 26 L. ed. 851; *Leinkauf v. Calman* (1888) 110 N. Y. 50, 17 N. E. 389 ("The doctrine that no corporate act can be binding without being in writing, or under the corporate seal, has long ceased to be maintained"). As to the modern English rule, see *Lawford v. Billericay etc. Council*, L. R. 1 K. B. (1903) 772 (implied contract) and note, 3 *Columbia Law Rev.*, 589.

(2) to borrow money and issue negotiable paper, if necessary and appro-

appropriate for transacting its business. *Bradbury v. Boston Canoe Club* (1891) 153 Mass. 77, 26 N. E. 132; *National Park Bank v. German-American etc. Security Co.* (1889) 116 N. Y. 281, 22 N. E. 567. Cf. *Bateman v. Mid-Wales R. Co.* (1866) L. R. 1 C. P. 499 (distinguishing railway co. from trading corporations); but see *Union Bank v. Jacobs* (1845) 6 Humph. (Tenn.) 514 ("if it may contract a debt, it necessarily may make provision for its payment, by drawing, or endorsing, or accepting notes or bills"). It has been held not appropriate for a savings bank to borrow money for investment purposes, *Franklin Co. v. Lewiston Savings Bank* (1877) 68 Me. 43, but appropriate to raise funds to avert a run on the bank. See also *National Bank v. Young* (1886) 14 Stew. Eq. (N. J.) 531.

(3) to acquire and convey property, if suitable and necessary for carrying on its business. *Co. Lit.* 44a, 300b; 1 Bl. Com. 478; 2 Kent Com. 281; *Stockton Savings Bank v. Staples* (1893) 98 Cal. 189, 32 Pac. 936; *Dupee v. Boston Water Power Co.* (1873) 114 Mass. 37; *Jones v. Guaranty & Co.* (1879) 101 U. S. 622, 25 L. ed. 1030. ("At the common law, every corporation had, as incident to its existence, the power to acquire, hold, and convey real estate, except so far as it was restrained by its charter or by act of parliament. This comprehensive capacity included also personal effects of every kind.") *In re Kingsbury Collieries, Ltd.*, L. R. 2 Ch. Div. (1907) 259 (power to sell implied).

A corporation, although its term of existence is limited, may hold a fee simple in real estate; *Nicoll v. New York etc. R. Co.* (1854) 12 N. Y. 121; and may hold a franchise extending beyond its own life. *Minneapolis v. Minneapolis etc. R. Co.* (1909) 215 U. S. 417, 54 L. ed. 259, 30 Sup. Ct. 118 (at termination of corporate life franchise is a divisible asset).

A railway, or other public-service corporation, has no power to alienate any of its property which is required for the performance of its duties. *Brunswick Gas Light Co. v. United Gas etc. Light Co.* (1893) 85 Me. 532, 27 Atl. 525 ("public or quasi public corporations, which possess and exercise the right of eminent domain, or its equivalent, owe duties to the public, as well as to their stockholders"); *Kean v. Johnson* (1853) 9 N. J. Eq. 401 (railroad cannot sell its entire property); *Thomas v. Railroad Co.* (1879) 101 U. S. 71, 25 L. ed. 950 (lease by railway co. of all its road, rolling-stock and franchises); *Central Transportation Co. v. Pullman's Palace Car Co.* (1890) 139 U. S. 24, 35 L. ed. 55, 11 Sup. Ct. 478. Otherwise as to property not essential to operation and service. *Union Pacific R. Co. v. Chicago etc. R. Co.* (1892) 51 Fed. 309, 2 C. C. A. 174.

(4) to pledge or mortgage its property, if necessary and appropriate for transacting its business. *Aurora etc. Horticultural Society v. Paddock* (1875) 80 Ill. 263; *Fidelity Trust Co. v. Louisville Gas Co.* (1904) 118 Ky. 588, 81 S. W. 927; *Jackson v. Brown* (1830) 5 Wend. (N. Y.) 590; *Jones v. Guaranty & Indemnity Co.* (1879) 101 U. S. 622, 25 L. ed. 1030 (mortgage for future advances); *In re Patent File Co.* (1870) L. R. 6 Ch. App. Cas. 83.

But not a railway or other public-service corporation, so far as its property requisite for the performance of its functions is concerned. *Commonwealth v. Smith* (1865) 10 Allen (Mass.) 449; *Lord v. Yonkers Fuel Gas Co.* (1885) 99 N. Y. 547, 2 N. E. 909 (valid as to real and personal property by statute, invalid as to franchises). Otherwise as to property not essential to operation. *Hendee v. Pinkerton* (1867) 14 Allen (Mass.) 381; *Union Pacific R. Co. v. Chicago etc. R. Co.* (1892) 51 Fed. 309, 2 C. C. 174. Railway and other public-service corporations today usually possess the power to mortgage by statute. See also *Quincy v. Chicago etc. R. Co.* (1880) 94 Ill. 537.

(5) to lend money or to lend credit by acting as surety or guarantor, but only if strictly necessary and appropriate to the corporate enterprise and not, in general, readily implied. *Kraft v. West Side Brewery Co.* (1906) 219 Ill. 205, 76 N. E. 372 (brewery co. has implied power to lend funds to saloon-keeper for purpose of erecting a saloon and hall where its product would be sold); *Holmes v. Willard* (1890) 125 N. Y. 75, 25 N. E. 1083, *semble* (manufacturing corporation may advance funds to manufacturer to enable

him to furnish goods); *Tod v. Kentucky Union Land Co.* (1893) 57 Fed. 47 (implied power to obligate itself as surety or guarantor "when it does so for its own benefit" founded on a valuable consideration), *affd.* (1894) 62 Fed. 335, 10 C. C. A. 393 (per Taft, J.), and followed, *Fidelity Trust Co. v. Louisville Gas Co.* (1904) 118 Ky. 588, 81 S. W. 927; *Winterfield v. Cream City Brewing Co.* (1897) 96 Wis. 239, 71 N. W. 101 (guarantee by brewing co. of payment of rent for hotel selling its beer upheld). But see *Best Brewing Co. v. Klassen* (1900) 185 Ill. 37, 57 N. E. 20 (corporation not authorized to sign appeal bond "in a case in which it had no direct interest"); *Leigh v. American Brake Beam Co.* (1903) 205 Ill. 147, 68 N. E. 713 (corporation organized to manufacture and sell railway appliances not authorized to lend); *Lucas v. White Line Transfer Co.* (1886) 70 Ia. 541, 30 N. W. 771 (corporation in "general freight and transfer business" not justified in becoming surety to brewing company for payments of beer by saloon); *Garrison Canning Co. v. Stanley* (1907) 133 Ia. 57, 110 N. W. 171; *Western etc. R. Co. v. Blue Ridge Hotel Co.* (1905) 102 Md. 307, 62 Atl. 351 (contract by which railroad co. guaranteed payment of interest and dividends on the bonds and stock of a hotel co. along the line of its road, *held, ultra vires*; the court saying, "A corporation has no power to enter into a contract of suretyship or guarantee, or otherwise lend its credit to another, unless the power is expressly conferred by its charter, or unless such a contract is reasonably necessary, or usual in the conduct of its business"); *Wheeler v. Everett Land Co.* (1896) 14 Wash. 630, 45 Pac. 316 (suretyship by custom); *Louisville etc. R. Co. v. Louisville Trust Co.* (1898) 174 U. S. 552, 43 L. ed. 1081, 19 Sup. Ct. 817 (guarantee by railroad co. of bonds of another, *ultra vires*).

(6) to act as trustee, *State v. Higby Co.* (1906) 130 Ia. 69, 106 N. W. 382; *Sheldon v. Chappell* (1888) 47 Hun (N. Y.) 59; *Vidal v. Girard's Exrs.* (1844) 2 How. (U. S.) 127, 11 L. ed. 205 (exploding the ancient ideas as "unsound and too artificial").

(7) to make reasonable by-laws, *Norris v. Staps* (1614-25) *Hobart's Rep.*, 210b, 211a; *Manufacturers etc. Bldg Co. v. Landay* (1905) 219 Ill. 168, 76 N. E. 146 (statutory).

(8) to make an assignment for the benefit of creditors, *Hutchinson v. Green* (1886) 91 Mo. 367, 1 S. W. 853 ("corporation may, like an individual, make an assignment"); *Coats v. Donnell* (1883) 94 N. Y. 168; *Vanderpoel v. Gorman* (1894) 140 N. Y. 563, 35 N. E. 932 ("exists inherently in all corporations unless specially forbidden").

(9) to make preferences in favor of certain creditors in the absence of a prohibitory statute, *Glover v. Lee* (1892) 140 Ill. 102, 29 N. E. 680; *Illinois Steel Co. v. O'Donnell* (1895) 156 Ill. 624, 41 N. E. 185 (good faith essential); *Nappanee Canning Co. v. Reid* (1902) 159 Ind. 614, 64 N. E. 870, 1115 (strong dissenting opinion); *Gould v. Little Rock etc. R. Co.* (1892) 52 Fed. 680 ("as unrestricted and absolute as is the common-law right of an individual to make preferences among his creditors").

(10) to take personal property by bequest, *Sherwood v. American Bible Society* (1864) 4 Abb. App. Dec. (N. Y.) 227, and equitable interests in realty by devise. See *Angell & Ames on Corporations*, sec. 178.

At common law, a corporation has no power to take by devise, nor under the original English Statute of Wills, 34 Hen. VIII, c. 5, nor under some of the Statutes of Wills in this country, e. g. New York. See *Stimson's Amer. Stat. Law*, sec. 2610.

A corporation not authorized to take realty by will by the laws of its own state may take by devise lands in another state where corporations generally are allowed so to take. *White v. Howard* (1871) 38 Conn. 342. But see *Starkweather v. American Bible Society* (1874) 72 Ill. 50, *contra*. Cf. *Thompson v. Swoope* (1855) 24 Pa. St. 474.

(11) A foreign corporation may in general do in any state whatever it is authorized by its charter to do, provided it is not contrary to any prohibitory law or the public policy of the state where the act in question is done. *Cowell v. Springs Co.* (1879) 100 U. S. 55, 25 L. ed. 547; *Christian Union v.*

Yount (1879) 101 U. S. 352, 25 L. ed. 888; Lancaster v. Amsterdam Improvement Co. (1894) 140 N. Y. 576, 35 N. E. 964.

For other cases of implied powers, see Henderson v. Bank of Australasia (1888) 40 Ch. Div. 170 (bank may pay five-year pension to family of deceased official); Taunton v. Royal Ins. Co. (1864) 2 H. & M. 135. (insurance co. may pay loss for which it is not legally liable); Richilieu Hotel Co. v. International Military Encampment Co. (1892) 140 Ill. 248, 29 N. E. 1044 (hotel co. authorized to subscribe to a fund to establish a military encampment likely to attract visitors), but *cf.* Davis v. Old Colony Railroad Co. (1881) 131 Mass. 258; Merchants etc. Improvement Co. v. Chicago etc. Bldg. Co. (1903) 106 Ill. App. 17 (broad construction); Lyndeborough Glass Co. v. Mass. Glass Co. (1873) 111 Mass. 315 (glass mfg. corporation possesses power to purchase and resell glass articles in order to retain its trade pending repairs); Freeman v. Sea View Hotel Co. (1898) 57 N. J. Eq. 68, 40 Atl. 218; Hennessy v. Muhleman (1899) 40 App. Div. (N. Y.) 175, 57 N. Y. S. 854; Leslie v. Lorillard (1888) 110 N. Y. 519, 18 N. E. 363; State v. Pittsburg etc. R. Co. (1903) 68 Oh. St. 9, 67 N. E. 93 (within implied powers of railway company to maintain and manage an accident and relief-fund department for its employees).

At common law a corporation has in general no implied power

(1) to transact any distinct and separate business not covered by its charter, or any business not incidental to, or consequential upon, its authorized business. Chewacla Lime Works v. Dismukes (1888) 87 Ala. 344, 6 So. 122; Stacy v. Glen Ellyn Hotel &c. Co. (1906) 223 Ill. 546, 79 N. E. 133 (hotel company unauthorized to engage in real estate business); Powell v. Murray (1896) 3 App. Div. (N. Y.) 273, 38 N. Y. S. 233 (corporation organized to manufacture electrical appliances not authorized to maintain a selling agency for products of another concern), *affd. short*, (1899) 157 N. Y. 717, 53 N. E. 1130; Pearce v. Madison etc. R. Co. (1858) 21 How. (U. S.) 441, 16 L. ed. 184 (purchase of steamboat and establishment of steamboat line by railway company).

(2) to make or indorse promissory notes for accommodation. J. G. Brill Co. v. Norton etc. R. Co. (1905) 189 Mass. 431, 75 N. E. 1090; Monument Nat. Bank v. Globe Works (1869) 101 Mass. 57 (enforceable in hands of a holder in due course); National Park Bank v. German-American etc. Security Co. (1889) 116 N. Y. 281, 22 N. E. 567; Pelton v. Spider etc. Lumber Co. (1903) 117 Wis. 569, 94 N. W. 293. See also Cook v. American Tubing etc. Co. (1906) 28 R. I. 41, 65 Atl. 641 ("a corporation has no implied power to issue or indorse bills or notes in which it has no interest for the mere accommodation of another"). That consent of all the stockholders may validate, see Martin v. Niagara Falls Paper Mfg. Co. (1890) 122 N. Y. 165, 25 N. E. 303.

(3) For other instances see, Matter of Co-operative Law Co. (1910) 198 N. Y. 479, 92 N. E. 15 (corporation cannot practise law); People v. Woodbury Dermatological Institute (1908) 192 N. Y. 454, 85 N. E. 697 (cannot practise medicine, statutory); State Electro-Medical Inst. v. State (1905) 74 Neb. 40, 103 N. W. 1078 (same); People ex rel Perkins v. Moss (1907) 187 N. Y. 410, 80 N. E. 383 (political contributions); and cases *infra*, Chap. V.—Eds.

CHAPTER V.

RIGHTS AND LIABILITIES ARISING OUT OF ULTRA VIRES TRANSACTIONS AS BETWEEN A CORPORATION AND NON-MEMBERS.

Section 1.—Ultra Vires Acquisition of Property.

ST. PETER'S R. C. CONGREGATION v. GERMAIN.

1882. 104 Ill. 440.¹

MR. JUSTICE MULKEY delivered the opinion of the court: The St. Peter's Roman Catholic Congregation brought to the February term, 1882, an action of ejectment, against Nicholas Germain, for the recovery of a valuable tract of land, situate in St. Clair county, consisting of about eighty acres. There was a judgment for the defendant in the court below, and the plaintiff brings the case here for review.

It appears, from a stipulation of the parties, that Catharine Agnes Germain, being the owner in fee of the premises, on the 2d day of November, 1878, executed and delivered to the plaintiff a deed therefor, properly acknowledged, and purporting to convey the same; that the plaintiff is, and was at the time of the conveyance, a religious corporation, organized and existing under the act of March 8, 1869, entitled "An act to provide for the holding of Roman Catholic churches, cemeteries, colleges, and other property;" and that at the time of said conveyance the plaintiff owned and occupied more than ten acres of land in St. Clair county, exclusive of the land described in the deed.

Under these facts the question is presented—and indeed this is the only question in the case—[whether the title to the land in dispute passed by the deed from Catharine Germain to the plaintiff.] No question is raised by counsel for the defendant in error as to the form or sufficiency of the deed, or the manner in which it was obtained, or with respect to the right or power of the grantor to convey, but the only question made is as to the capacity of the plaintiff in error to take under the deed. The determination of this question depends upon the construction that must be given to the statutes then in force authorizing religious corporations to acquire lands in this state. By the 2d section of the act of 1869, above mentioned, religious societies organized under it are authorized "to receive, hold, dispose of, and convey, any kind of property," and by the 10th section the

¹ Slight portion of opinion omitted.—Eds.

act is declared to be "subject to any limitation or modification which may hereafter be enacted by general law as to the amount of real estate to be held by the corporations, respectively, provided for herein." It will be perceived this act contains no limitation as to the quantity of lands religious societies incorporated under it may "receive" and "hold", but, as we have just seen, the legislature, by the 10th section reserves the right to limit and modify the amount "to be held" by them. At the time of the adoption of this act the 44th section of chapter 35, Revised Statutes 1845, entitled "Corporations", was in force, which authorized any religious society or corporation then existing, or which might thereafter be formed, "to receive, by gift, devise or purchase, any quantity of land not exceeding ten acres," etc. This act continued in force until in 1872, when it was repealed, and section 42, of chapter 32, of the present revision, was adopted in its stead, which provides that "any corporation that may be formed for religious purposes under this act, or under any law of this state, for the incorporation of religious societies, may receive, by gift, devise or purchase, land not exceeding ten acres," etc. By comparing the two sections it will be perceived that so far as the present inquiry is concerned, they are substantially the same, so that the adoption of the latter section was in effect merely continuing in force the former. * * *

In the light of judicial history, and the legislation of this country on the subject, we cannot for a moment believe that it was the intention of the legislature to put it in the power of any religious society or corporation to acquire lands to any indefinite extent as is claimed here. It has ever been the policy of this country, including our own state, to keep landed estates as much unfettered as possible, so that their free transfer from one person to another may not be interrupted or hindered, and it will not be denied that to permit corporations to acquire real estate to an unlimited extent would be destructive of this policy. Under the legislation of our state, which we have been considering, a religious corporation is authorized to receive or acquire lands to the extent of ten acres, and no more. Any amount in excess of that is expressly forbidden by the statute, and it follows that all the conveyances, deeds or other contracts made in violation of this prohibition, are absolutely void.

It is a well settled rule that where a corporation is forbidden to take or receive lands, such a prohibition goes to its capacity to acquire, and a deed made to it under such circumstances passes no title, such a conveyance being absolutely void; and the correctness of this rule is conceded by the learned counsel for plaintiff in error. It is claimed, however, this rule only applies where the prohibition is total, and not merely partial, as in this case,—that where there is a capacity to take to a limited extent, and a conveyance is made for quantity in excess of that which the law permits, the title will nevertheless pass to the whole, subject to the right of the state to interpose for the excess. We cannot give our adhesion to this doctrine,

for it would be conceding that a corporate body might clothe itself with the legal title to an estate in contravention of an express provision of the statute, which is inconsistent with well recognized principles. Whether a deed of that kind would be good for the amount of land that might lawfully be conveyed, and inoperative for the residue, or whether it would be regarded as void for uncertainty as to what particular ten acres passed by it, it is not necessary for us to stop to inquire, for whatever might be the rule in such a case, it could have no application to the one before us. Here it is admitted the plaintiff in error had, previous to the conveyance of the land in dispute, already acquired, and was then the owner of ten acres of land,—the outside limit it was permitted to take. This being so, it is clear its capacity to acquire other lands was fully exhausted, and there was a total want of power to take the land in question.

Moreover, we are of the opinion that conceding the act of 1869 was not adopted subject to the limitation contained in the 44th section of the act of 1845, as we have seen it was, nevertheless, the reservation, in the 10th section of the former act, of the power to regulate by general law the amount or quantity of land which corporations organized under it might hold, fully authorized the legislature—assuming the power did not exist independently of it—to prescribe the amount or quantity of land which such corporations might take or acquire. If the legislature has the power—and this is conceded—to say these organizations shall not hold to exceed a specified number of acres of land, we are of the opinion, as the most effectual way of enforcing such power, it may say they shall only take or acquire the specified quantity.

Leaving out of view the legal aspects of the question, it looks like a great hardship that the purposes of the grantor in the deed should be thus thwarted, and that the church should be deprived of the estate so generously attempted to be given to it; yet such considerations must not be permitted to disturb the balance of the scales of legal justice. *Ita lex scripta est*, and it is the duty of all to submit to its mandate, and we are assured that none will do so more cheerfully than the plaintiff in this case.

The judgment of the circuit court is affirmed.

Judgment affirmed.

MR. JUSTICE CRAIG: I do not concur in the decision of this case. The St. Peter's Roman Catholic Congregation, a corporation existing by law, under our statute had authority to take and hold lands by deed or devise, and whether it has exceeded its power in accepting a conveyance of the land in question, can, in my judgment, only be inquired into by the state. The question is one between the corporation and the sovereign power, in which individuals have no concern. *De Camp v. Dobbins*, 29 N. J. Eq. 36.

MR. JUSTICE DICKEY: I concur with the view expressed by Mr. Justice Craig.²

² Cf. *Hamsher v. Hamsher* (1890) 132 Ill. 273, 23 N. E. 1123: "If the

KERFOOT v. FARMERS' & MERCHANTS' BANK.

1910. 218 U. S. 281, 54 L. ed. 1042.

THE facts, which involve the validity of a transfer of real estate to a national bank, are stated in the opinion.

MR. JUSTICE HUGHES delivered the opinion of the court.

This action was brought in 1894, in the Circuit Court of Grundy County, state of Missouri to set aside a deed of real property made by James H. Kerfoot to the First National Bank of Trenton, Missouri, and also a deed by which that bank purported to convey the same property to the defendants, Hervey Kerfoot, Alwilda Kerfoot and Lester R. Kerfoot, and for the recovery of possession. The plaintiffs in the action, which was brought shortly after the death of James H. Kerfoot, were Homer Hall, administrator of his estate, and Robert Earl Kerfoot, his infant grandson, who claimed to be his only heir at law and sued by Homer Hall as next friend. The petition contained two counts, one in equity, the other in ejectment. Upon the trial the Circuit Court found the issues for defendants and the judgment in their favor was affirmed by the Supreme Court of Missouri. 145 Missouri 418. On his coming of age Robert Earl Kerfoot sued out this writ of error.

The plaintiff in error challenges the conveyance made by James H. Kerfoot to the bank, upon the ground that under § 5137 of the Revised Statutes of the United States, relating to national banks, the bank was without power to take the property, and hence that no title passed by the deed, but that it remained in the grantor and descended to the plaintiff in error as his heir at law. It appears that the deed, which was absolute in form, with warranty and expressing a substantial consideration, was executed in pursuance of an arrangement by which the title to the property was to be held in trust to be conveyed upon the direction of the grantor; and the Supreme Court of Missouri decided that a trust was in fact declared by the grantor in favor of Hervey, Alwilda and Lester R. Kerfoot, to whom ran a quitclaim deed, which he prepared and forwarded to the bank to be signed and acknowledged by it and then returned to him.

Young Men's Christian Association of Decatur 'has exceeded in extent its power of holding real estate, appellant, we conceive, cannot take advantage of the fact' (Alexander v. Tolleston Club, 110 Ill. 65.) Where a corporation may, for some purposes, acquire and hold the title to real estate, it cannot be made a question by any party, except the State, whether the real estate has been acquired for the authorized uses or not. (Hayward v. Davidson, 41 Ind. 214.) There being capacity to purchase or to receive by devise, whether the corporation, in so purchasing or receiving, exceeds its power is a question between it and the State, and does not concern appellant."

See also Barnes v. Suddard (1886) 117 Ill. 237, 7 N. E. 477; Rector v. Hartford Deposit Co. (1901) 190 Ill. 380, 60 N. E. 528 (distinguishing total want, from abuse, of powers); Hayden v. Hayden (1909) 241 Ill. 183, 89 N. E. 347.—Eds.

But while the purpose of this transaction was not one of those described in the statute for which a national bank may purchase and hold real estate, it does not follow that the deed was nullity and that it failed to convey title to the property.

In the absence of a clear expression of legislative intention to the contrary, a conveyance of real estate to a corporation for a purpose not authorized by its charter, is not void, but voidable, and the sovereign alone can object. Neither the grantor nor his heirs nor third persons can impugn it upon the ground that the grantee has exceeded its powers. *Smith v. Sheeley*, 12 Wall. 358; *National Bank v. Matthews*, 98 U. S. 621; *National Bank v. Whitney*, 103 U. S. 99; *Reynolds v. Crawfordsville Bank*, 112 U. S. 405; *Fritts v. Palmer*, 132 U. S. 282; *Leazure v. Hillegas*, 7 Serg. & R. (Pa.) 313. Thus, although the statute by clear implication forbids a national bank from making a loan upon real estate, the security is not void and it cannot be successfully assailed by the debtor or by subsequent mortgagees because the bank was without authority to take it; and the disregard of the provisions of the act of Congress upon that subject only lays the bank open to proceedings by the Government for exercising powers not conferred by law. *National Bank v. Matthews*, supra; *National Bank v. Whitney*, supra; *Swope v. Lefingwell*, 105 U. S. 3.

In *National Bank v. Matthews*, supra, viewing that case in this aspect, the court said:

"The opinion of the Supreme Court of Missouri assumes that the loan was made upon real-estate security within the meaning of the statute, and their judgment is founded upon that view. These things render it proper to consider the case in that aspect. But, conceding them to be as claimed, the consequence insisted upon by no means necessarily follows. The statute does not declare such a security void. It is silent upon the subject. If Congress so meant, it would have been easy to say so; and it is hardly to be believed that this would not have been done, instead of leaving the question to be settled by the uncertain result of litigation and judicial decision. Where usurious interest is contracted for, a forfeiture is prescribed and explicitly defined.

* * * * *

"Where a corporation is incompetent by its charter to take a title to real estate, a conveyance to it is not void, but only voidable, and the sovereign alone can object. It is valid until assailed in a direct proceeding instituted for that purpose. *Leazure v. Hillegas*, 7 Serg. & R. (Pa.) 313; *Goundie v. Northampton Water Co.*, 7 Pa. St. 233; *Runyon v. Coster*, 14 Pet. 122; *The Banks v. Poitiaux*, 3 Rand. (Va.) 136; *McIndoe v. The City of St. Louis*, 10 Missouri 575, 577. See also *Gold Mining Co. v. National Bank*, 96 U. S. 640."

This rule, while recognizing the authority of the Government to which the corporation is amenable, has the salutary effect of assuring the security of titles and of avoiding the injurious consequences

which would otherwise result.¹ In the present case a trust was declared and this trust should not be permitted to fail and the property to be diverted from those for whom it was intended, by treating the conveyance to the bank as nullity, in the absence of a clear statement of legislative intent that it should be so regarded.

The cases in this court, which are relied upon by the plaintiff in error, are not applicable to the facts here presented and are in no way inconsistent with the doctrine to which we have referred. *McCormick v. Market Bank*, 165 U. S. 538; *California Bank v. Kennedy*, 167 U. S. 362; *Concord First National Bank v. Hawkins*, 174 U. S. 364.

It was also urged by the plaintiff in error that the deed was not accepted by the bank, and was inoperative for that reason. The Supreme Court of Missouri *held* upon the evidence that it was accepted, and this court, on a question of that character, does not review the findings of fact which have been made in the state court. *Waters-Pierce Oil Co. v. State of Texas*, 212 U. S. 86; *Egan v. Hart*, 165 U. S. 188; *Clipper Mining Co. v. Eli Mining & Land Co.*, 194 U. S. 220.

Assuming that the deed was accepted by the bank, it was effective to pass the legal title, and the plaintiff in error as heir at law of the grantor cannot question it.

Judgment affirmed.²

JOHN V. FARWELL CO. v. WOLF.

1897. 96 Wis. 10, 70 N. W. 289.⁴

APPEAL from a judgment of the Circuit Court for Juneau County: O. B. Wyman, Circuit Judge. Reversed.

Action to recover damages for an alleged conspiracy to defraud. The complaint sets forth, in substance, that in the summer of 1893 defendants entered into a fraudulent conspiracy to defraud wholesale dealers in goods, wares and merchandise; that the scheme agreed upon was that defendant Moses Josephson should purchase goods of such dealers on credit, without any intention of paying for

¹*De Witt County Nat. Bank v. Mickelberry* (1910) 244 Ill. 77, 91 N. E. 86; *Nantasket Beach Steamboat Co. v. Shea* (1902) 182 Mass. 147, 65 N. E. 57; *Benton v. City of Elizabeth* (1898) 61 N. J. L. 411, 39 Atl. 683, 906, *affd.*, (1898) 61 *ibid.* 693; *Burden v. Burden* (1899) 159 N. Y. 287, 54 N. E. 17; *Leazure v. Hillegas* (1821) 7 S. & R. (Pa.) 313 (defeasible title passes subject to escheat); *Advance Thresher Co. v. Rockafellow* (1903) 16 S. Dak. 462, 93 N. W. 652; *Puget Sound Nat. Bank v. Fisher* (1909) 52 Wash. 246, 100 Pac. 724; *National Bank v. Matthews* (1878) 98 U. S. 621, 25 L. ed. 188; *Fritts v. Palmer* (1889) 132 U. S. 282, 33 L. ed. 317, 10 Sup. Ct. 93; *Blair v. City of Chicago* (1905) 201 U. S. 400, 50 L. ed. 801, 26 Sup. Ct. 427, *Accord.* *Occum Co. v. Sprague Mfg. Co.* (1868) 34 Conn. 529 (*semble*), *Contra.*—Eds.

⁴Portion of opinion omitted.—Eds.

the same, have the same delivered at his store in New Lisbon, Wisconsin, and that the same should then be sold, conveyed away, and concealed in such a way that the proceeds might be divided between the co-conspirators; that pursuant to such conspiracy, in August and September, 1893, goods, wares and merchandise to the amount of \$434.83 were purchased of plaintiff in the name of said Josephson, were delivered to him, and disposed of for the benefit of the defendants pursuant to the aforesaid fraudulent scheme; that no part of such goods has been paid for, and that by reason of the facts plaintiff has been damaged in the said sum of \$434.83 and interest; that, further, in pursuance of said fraudulent conspiracy, goods, wares, and merchandise were at various times during the year 1893, particularly stated, purchased of some twenty-four different persons, co-partnerships, and corporations, the name of each being given with the amount purchased; and all of such goods were delivered to said Josephson and disposed of for the benefit of the defendants pursuant to the aforesaid fraudulent scheme, no part of which has been paid for, to the damage of the sellers to the amount of their respective sales and interest; that before the commencement of this action such sellers, for a valuable consideration to them respectively paid, sold, assigned, and conveyed to plaintiff their respective claims for goods so sold and delivered, together with their respective causes of action for damages against defendants on account of the aforesaid conspiracy. The aggregate of plaintiff's claim for damages for goods procured of it pursuant to the aforesaid fraudulent scheme, and of the several other claims mentioned, amounted to \$5,102.32, for which sum judgment was demanded, with interest. The defendants, except Josephson, joined in an answer to the complaint.

The result of the trial was that the jury found for the plaintiff on all the issues, and assessed the damages at the full amount claimed which, with interest, made \$5,432.25. Proceedings were duly had on the trial, and subsequent thereto, requisite to preserve for review the questions discussed in the opinion. Judgment was rendered on the verdict, and defendants appealed.

MARSHALL, J.—The record shows that plaintiff is a corporation organized for the purpose of carrying on a general dry goods business. The point was raised on the trial, and preserved for review, that it did not possess power to acquire by assignment claims for damages in no way connected with its own affairs, growing out of the alleged conspiracy to defraud. It does not appear that such claims were in any way necessary to the preservation or enforcement of plaintiff's original claim, or that such purchase was to effect in any way the purposes of its organization, so as to bring its action in that regard within the rules that a corporation may, to preserve its own property and protect its legitimate interests, acquire and enforce liens which would otherwise be outside of the purposes of its organization. A corporation has only such powers as its organic act, charter, or articles of organization confer. This is elementary, but it

includes such powers as are reasonably necessary to effect all the general purposes of the corporate creation, though not particularly specified in its charter, unless prohibited thereby or by some law of the state. From the foregoing, without further discussion, we must hold that plaintiff had no authority to acquire by purchase the various claims for damages on which a recovery was had. But it by no means follows that its want of power can be taken advantage of by the defendants in this action. Formerly want of corporate power was an effective weapon, both for defense and attack, in the hands of private parties; but, without any change whatever respecting the general doctrine of *ultra vires* as applied to the acts of corporations acting outside the purposes of their creation, there has been a gradual development in the direction of holding that none but a person directly interested in the corporation, or the state, can question such authority. Such development from the rigorous rule which anciently obtained was manifested earliest in the adoption of the rule that, where a corporation has violated its charter in the purchase and acquirement of real estate, its title thereto and right to enjoy the same cannot be inquired into collaterally in actions between private parties or between the corporation and private parties;—that it can be questioned only by the state. *Natoma W. & M. Co. v. Clarkin*, 14 Cal. 544; *Alexander v. Tolleston Club*, 110 Ill. 65; *Fritts v. Palmer*, 132 U. S. 282; *Runyan v. Coster's Lessee*, 14 Pet. 122; *National Bank v. Whitney*, 103 U. S. 99; *Shewalter v. Pirner*, 55 Mo. 218; *Ragan v. McElroy*, 98 Mo. 349; *National Bank v. Matthews*, 98 U. S. 621. In the latter case the Supreme Court of the United States, reversing the Supreme Court of the state of Missouri, laid down the rule, "where a corporation is incompetent by its charter to take a title to real estate, a conveyance to it is not void, but only voidable, and the sovereign alone can object;" that "it is valid until assailed by a direct proceeding instituted for that purpose" by the government; and, further, in effect, that the danger of a judgment of ouster and dissolution is the only check to prevent and punish violations of corporate charters. If the question were respecting the right of a private person to challenge corporate action concerning the acquirement or enjoyment of lands without authority in the charter so to do, it would be deemed so well settled that no such right exists as not to be opened to serious discussion; but whether the same rule governs generally is not so clear.

An extended discussion of the subject, showing the process of development in the application of such rule, would be interesting and instructive, but not necessary for the purposes of this opinion. Therefore we content ourselves with referring to a few well-considered cases, showing the present state of the law respecting the subject, which Thompson, in his work on Corporations, very properly refers to as a "new and growing doctrine." In *Prescott Nat. Bank v. Butler*, 157 Mass. 548, an action between the bank and a private

person, the question was raised of whether the action of the former in purchasing notes in the open market as a commodity was ultra vires; and in respect thereto the court said, in effect, that if such purchase be ultra vires, it is not made penal or expressly prohibited; therefore the violation of law could be remedied only in proceedings against the bank, in the name of the state, to deprive it of its charter. In *Grant v. Henry Clay C. Co.*, 80 Pa. St. 208, where the question was whether the corporation could purchase or hold leases of mining lands, the court, in deciding such question, said, in effect, that if the commonwealth is interested in such an inquiry it must be made by the proper officer; that the question was of a public nature, concerning solely the sovereignty of the state, and not one that in any way concerned private parties. In *Martindale v. K. C., St. J. & C. B. R. Co.*, 60 Mo. 508, the question was whether the defendant had violated statutory requirements, and the court laid down the broad doctrine that collateral inquiry by a private citizen into the supposed illegal acts of a corporation is not permitted in any case, unless expressly so provided by statute. To the same effect are *Kinealy v. St. L., K. C. & N. R. Co.*, 69 Mo. 658, and *Hovelman v. Kansas City H. R. Co.*, 79 Mo. 632. In *Baker v. N. W. G. L. Co.*, 36 Minn. 185, the question was whether the purchase and enforcement of certain mortgage liens was in excess of the corporate authority. *Held*, that none but the state or a stockholder could raise the question.

If the position that the principle under discussion is now, in most jurisdictions, recognized as one of general application, except in respect to contracts wholly executory, required further support, resort might be had to many other adjudications of the highest respectability, though authorities there are which still adhere to the old rule that a corporate act in excess of its power, either because outside of the purposes of the corporation or because prohibited by statute, is ultra vires, and cannot be enforced in any action in any court of justice, without regard to whether such act be challenged by the public or by a private person. Such authorities are exceptional. Judge Thompson, in his valuable treatise on the Law of Corporations (volume 5), commenting on the subject (secs. 6033-6038), appears to deprecate the prevalence of the "new doctrine," and to argue against its further extension, upon the ground that it practically destroys the effect of the doctrine of ultra vires, as applied to the unauthorized exercise of corporate power; but the learned author is manifestly in error in that respect. Such doctrine, notwithstanding the limitation which modern development has placed on the means by which it may be called into use, still exists, and may and will continue to exist, adapted as fully as ever to restrain the abuse of corporate franchises and authority, and to punish such abuse whenever the state, in its sovereign capacity, sees fit to exercise it. That such doctrine cannot be resorted to as a weapon for attack and defense in the hands of mere private persons, and used as a ready

means of embarrassing business operations by and with corporate bodies, which directly or indirectly touch and administer to human desires at every turn of the individual in modern life, while its effectiveness for all essential purposes of restraint and punishment is fully preserved, furnishes no cause for regret, but rather cause for gratification at the evidence of how certainly principles, by natural growth and development, adapt the law and its administration to the ever-changing needs of advancing civilization, so as best to promote justice and the common welfare. When a corporation offends against the law of its creation, such offense is against the sovereignty of the state; hence it is most proper that the state should apply the remedy and be charged with the sole responsibility in that regard, and such is the law by the trend of modern authorities, which we approve. This does not hold but that a person directly interested as a stockholder may, in a proper case, interfere, or but that the court may refuse on its own motion, or the objection of a private person, to aid a corporation to enforce, or protect it from the effect of, a contract wholly executory, when outside the purposes of the corporate organization.

In accordance with the foregoing, we hold that if a corporation purchases, pays for, and takes an assignment of a cause of action respecting matters outside the purposes of its creation and not authorized by its charter, in any action to enforce such cause of action want of corporate power to engage in such business cannot be interposed as a defense. * * *

*Judgment reversed.*⁵

MERCHANTS' NAT. BANK v. WEHRMANN.

1905. 202 U. S. 295, 50 L. ed. 1036.

MR. JUSTICE HOLMES delivered the opinion of the court.

This is a bill for the dissolution of a partnership, a receiver and an account. The partnership was formed to purchase, improve, divide into lots and sell a leasehold. There were forty shares in the firm, represented by transferable certificates. The plaintiff in error took nine of these shares as security for a debt, and afterwards became the owner of them in satisfaction of the debt, subject to the question whether the transaction was within the powers of a national

⁵State Ins. Co. v. Farmers' Mutual Ins. Co. (1902) 65 Neb. 34, 90 N. W. 997; Peru Plow & Implement Co. v. Harker (1906) 144 Fed. 673, 75 C. C. A. 475 (executed assignment of cause of action), *Accord*.

As to the passing of title in cases of *ultra vires* acquisition of tangible personal property, see *Morris v. Hall* (1868) 41 Ala. 510; *Edwards v. Fairbanks* (1875) 27 La. Ann. 449 ("the purchase by the company transferred the title"); *Parish v. Wheeler* (1860) 22 N. Y. 494; *Bank v. Bank of Victoria* (1871) L. R. 3 Pr. Coun. App. Cas. 526.—Eds.

bank. It was found at the trial that the partners must contribute to pay the debts of the firm, and some of them being insolvent, the bank was charged with the full share of a solvent partner. The Supreme Court of the state held this to be wrong, but decided that the bank became a part owner of the property and that, as it joined in the management of the same, it was liable for nine-fortieths of the expenses, which constituted the debts of the firm. 69 Ohio St. 160. A decree was entered to that effect, and the bank brought the case here. * * *

The question of substantive law presented is not without difficulty. It is not disposed of by the general proposition that a national bank may take by way of security property in which it is not authorized to invest, and may become owner of it by foreclosure or in satisfaction of a debt. It is not disposed of even by the decisions that it may acquire stock in a corporation in this way, *First National Bank of Charlotte v. National Exchange Bank*, 92 U. S. 122, and so subject itself to the liability of a stockholder for the corporate debts. *National Bank v. Case*, 99 U. S. 628; *California Bank v. Kennedy*, 167 U. S. 362, 366, 367; *First National Bank of Ottawa v. Converse*, 200 U. S. 425, 438, a proposition not shaken by *Scott v. Deweese*, 181 U. S. 202, 218. For it does not follow that because the interest in a partnership is represented by a paper certificate in form more or less resembling a certificate of stock in a corporation and transferable like it, a national bank can take the partnership certificate to the same extent that it could take the stock.

As the Supreme Court of Ohio assumes such partnerships and certificates to be valid we assume them to be. *Wells v. Wilson*, 3 Ohio 425; *Walburn v. Ingilby*, 1 Myl. & K. 61, 76; *Re The Mexican & South American Co.*, 27 Beav. 474, 481; S. C., 4 De G. & J. 320; *Philips v. Blachford*, 137 Massachusetts, 510. We may assume further, in accordance with a favorite speculation of these days, that philosophically a partnership and a corporation illustrate a single principle, and even that the certificate of a share in one represents property in very nearly the same sense as does a share in the other. In either case the members could divide the assets after paying the debts. But from the point of view of the law there is a very important difference. The corporation is legally distinct from its members, and its debts are not their debts. Therefore, when a paid-up share in a corporation is taken, no liability is assumed, apart from statute, but simply a right equal in value to a corresponding share in the assets and good will of the concern after its debts are paid. If the right is worth something it is a proper security, and if it is worth nothing no harm is done. It is true that statute may add a liability, but when, as usual, this is limited to the par value of the stock it has not been considered to affect the nature of the share so fundamentally as to prevent a national bank from taking it in pledge, with qualifications, as it might take land or bonds.

But to take a share by transfer on the books means to become a

member of the concern. The person who appears on the books of the corporation as the stockholder is the stockholder as between him and the corporation, and his rights with regard to the corporate property are incident to his position as such. *National Bank v. Case*, 99 U. S. 628, 631; *Pullman v. Upton*, 96 U. S. 328. This does not matter, or matters less, in the case of a corporation, for the reasons which we have stated. But when a similar transfer is made of a share in a partnership it means that the transferee at once becomes a member of the firm and goes into its business with an unlimited personal liability, in short, does precisely what a national bank has no authority to do. This the Supreme Court of Ohio rightly held beyond the powers of the bank. U. S. Rev. Stat., §§ 5136, 5137. It is true that it has been held that a pledgee may escape liability if it appears on the certificate and books that he is only a pledgee. *Pauly v. State Loan & Trust Co.*, 165 U. S. 606; *Robinson v. Southern National Bank*, 180 U. S. 295; *Rankin v. Fidelity Trust Co.*, 189 U. S. 242, 249. No doubt the security might be realized without the pledgee ever becoming a member of the firm. It is not necessary in this case to say that shares like the present could not be accepted as security in any form by a national bank. But such a bank cannot accept an absolute transfer of them to itself. It recently has been decided that a national bank cannot take stock in a new speculative corporation, with the common double liability, in satisfaction of a debt. *First National Bank of Ottawa v. Converse*, 200 U. S. 425. A fortiori, it cannot take shares in a partnership to the same end.

We are of opinion that with the liability as partner all liability falls. The transfer of the shares to the bank was not a direct transfer of a legal interest in the leasehold, which was in the hands of trustees. It was simply a transfer of a right to have the property accounted for and to receive a share of any balance left after paying debts, and the acquisition of this right was incident solely to membership in the firm. If the membership failed the incidental rights failed with it, and with the rights the liabilities also disappeared. Becoming a member of the firm was the condition of both consequences. As the bank was not estopped by its dealings to deny that it was a partner, it was not estopped to deny all liability for partnership debts.] See *California Bank v. Kennedy*, 167 U. S. 362, 367. It seems to us unnecessary to add more in order to show that the claim against the plaintiff in error must be dismissed.

Judgment reversed.

MR. JUSTICE HARLAN, MR. JUSTICE BREWER and MR. JUSTICE McKENNA dissent.*

* In *California Bank v. Kennedy* (1897) 167 U. S. 362, 42 L. ed. 198, held that the want of authority to purchase the stock of another corporation may be set up by a national bank to defeat an attempt to enforce against it the liability of a stockholder, "the transaction being absolutely void." So also, *In re European Society Arbitration Acts*, L. R. 8 Ch. Div. (1878) 679. But see *Holmes etc. Mfg. Co. v. Holmes etc. Metal Co.* (1891) 127 N. Y. 252,

FARRINGTON v. PUTNAM.

1897. 90 Maine 405, 37 Atl. 652.¹

THIS was a bill in equity by and on behalf of certain heirs of Ira P. Farrington, deceased, against the executors, the Main Eye and Ear Infirmary, and the other heirs. The deceased by his will devised and bequeathed a large part of his estate to the Maine Eye and Ear Infirmary, a charitable association organized under a general statute of Maine. This statute provided (R. S. c. 55, sec. 4): "Such corporations may take and hold by purchase, gift, devise or bequest, personal or real estate, in all not exceeding one hundred thousand dollars in value, owned at any one time, and may use and dispose thereof only for the purposes for which the corporation was organized." The bill alleged that the infirmary had, at the death of testator, property to the full amount of one hundred thousand dollars in value and was incompetent to receive any more. The executors and infirmary demurred to the bill. The demurrers were sustained and the bill dismissed, to which plaintiffs excepted.

PETERS, C. J. * * *

The question on the first branch of the case, therefore, is whether these devises and bequests are absolutely void as the complainants contend, or whether they are merely voidable according to the view of the question taken by the respondents. After very much examination of the authorities pro and con, and careful consideration of the principles which affect the respective positions of the parties, we feel forced to the conclusion that the position advocated by the complainants ought not to be sustained. We feel very much impressed with the theory, stated in many of the cases, that a charter is a contract between the state and the corporation; and that for any misuse or abuse of its privileges or powers the corporation is amenable to the state only, no individual having anything to do with the question. As applicable to the present case, the principle is that, if the infirmary, by accepting these bequests and devises, increases its property ever so much in excess of the amount in value which the statute allows it to possess, it would be a transgression of the law which the state can prosecute or not as it pleases, and the heirs of the testator have no interest therein. As long as the state does not interfere for the violation, it waives it and permits the infirmary to retain the property.

The general statute under which this infirmary was organized is not expressly prohibitory, but rather regulative and directory. No penalties are attached and none intended more than a possible forfeiture of the excessive property received, or of the charter, or of one or both. This interpretation of the statute cannot by any pos-

27 N. E. 831 (*semble*), *contra*. Cf. National Bank v. Case (1878) 99 U. S. 628, 25 L. ed. 448.—Eds.

¹ Statement rewritten. Portions of opinion omitted.—Eds.

sibility be harmful to the community, as the state can make it as stringent as it pleases at any time. But thus far the state has had no motive either to amend the statute or to enforce forfeitures for violation of its provisions. And in one section of the chapter relating to general organizations the legislature allows devises, bequests and gifts to towns for the establishment, or increase of public libraries, without imposing any limitation whatever. R. S. Ch. 55, § 10. There cannot be an objection that such absorption of property excludes capital from taxation, because that is a matter wholly within the control of the legislature.

An overstrict construction of the law and of the rights of parties under the law in the case before us is neither expedient nor reasonable. Here is an institution, and the only one of the kind in the state, and virtually a state charitable institution of the most beneficent and humane kind, seeking money for supporting its very life and existence, and to enable it to render assistance free of charge to the poor of the state suffering from diseases of the eye and ear. The testator, who had been always a director in the institution and finally its president, knowing and fully appreciating its condition and necessities, after making provisions for other local charities, and giving to his next of kin preferred bequests according to his own judgment as to what they should have out of his estate, made, not while in the extremities of sickness, but nearly five years before his death, these legacies and devises for the use of the infirmary. Presumably he and those whose assistance he obtained to aid him in executing his purposes never dreamed that there was any obstacle in the way of his giving or the infirmary receiving the bounties which he so strongly desired to be charitably expended. And now what a spectacle is presented if equity be successfully invoked to take advantage of this accident or mistake; equity, whose boasted vocation is to relieve against accident and mistake, in order to wrest from this institution these donations for the benefit of distant relatives and heirs! What a public misfortune it would have been, if on account of the limited amount of capital it is by its charter privileged to hold, it had turned out that our oldest college in this state was prevented from receiving the munificent bequests lately tendered to it by deceased citizens of the states of California and New York, such donations not having as yet been actually received, and the state itself powerless to allow the college to take the gifts merely on account of such limitation!

It will be noticed that most of the authorities, on which the complainants rely, concede that the rule which we would apply to devises is at all events applicable to gifts by deed, the argument being that in such a case as this a deed would be valid and a devise void. It seems inconsistent that such potential consequences should attach to the mere form of transmitting the property. We do not appreciate the justice of saying that a deed of property delivered by a donor on the day of his death to a corporation would be good, and a devise

of the same property made on the same day would be bad. But the argument by the complainants is that, in the one case, the transaction is executed and, in the other case, that it cannot be considered as executed without a resort to the forms and assistance of the courts. We think the whole thing involves a distinction without a difference, a formal but not substantial distinction. Each mode of transfer needs the protection and aid of the law to render it operative. In the first place, the will must be probated, it is said. [But on that question no inquiry can be instituted to see if there be any impropriety in any particular devise or bequest.] The residuary bequest in this will is fair and proper on its face, and that is all that is required. The act of probating the will is the probating of all its parts. A devise of real estate vests such estate at once in the devisee, the title of such devisee being liable to be defeated if the estate be necessary for the payment of debts or the expenses of administration. Section 15, Ch. 74, R. S., reads as follows: "No will is effectual to pass real or personal estate unless proved and allowed in the probate court." This will has been approved by the probate courts below and above with no questions or exceptions thereto pending. But it is said the bequest of the personal estate cannot be carried into effect until a distribution has been ordered and the executors' accounts have been approved. We think that even this fine technicality may be avoided by the executors, if need be. They would be justified in paying all the property left in their hands as residuary estate without any order therefor, should the devisees be willing to accept it and discharge the executors from their responsibilities. A good many estates are settled by the parties interested without any aid or order from the probate court.

The foregoing reasoning only serves to illustrate the unsubstantial foundation upon which it is endeavored to raise a technical excuse for pronouncing a deed voidable and a devise absolutely void. The true and conclusive answer, however, to this indefensible position of the complainants is that it is utter assumption on their part in declaring a devise like this to be void, when it is voidable merely, and can be rendered void in no way other than by the act of the government itself. No wrongful act by a corporation renders its charter void or creates any forfeiture without proceedings by which such forfeiture shall be established. A cause for forfeiture is not itself forfeiture. The same section which prescribes the amount of property which this corporation may hold, also declares that it may use and dispose of the same for the purpose for which it was organized. Suppose the corporation wrongfully uses or disposes of its property, could any party but the state intervene to punish the corporation for such transgression?

Now what is there illegal, let us ask, in this court or in the probate court below acting in the furtherance of bequests that are simply voidable and consequently valid until they have been declared to be

otherwise upon the intervention of the state? If the state has the exclusive privilege, as it has, of rendering the voidable bequest void, what is there wrongful in our regarding it as sound and sufficient while the question of its validity is not acted upon by the state, or the error is waived or permitted by the state? What right has the judicial branch of the government to dictate what the state should do against its will or its policy, and decide a question for the state which the state can better decide for itself? What right has the court to deprive the state of all opportunity to determine whether it will thus severely punish this corporation for the mistake of the testator or will waive or overlook it? Certainly the state should not be prevented from making such election. If courts at the instigation of heirs can refuse to act upon voidable bequests as valid until avoided by the state, then, as a matter of course, the state can practically never have any opportunity to exercise its discretion in such a case any more than as if such right never existed, and the court would be assuming the prerogative of really acting in opposition to the state. The court could not exercise any broad discretion in the solution of the question, while the state could. It certainly is an excellent policy to refer such questions to the discretionary power of the state, which can determine them, according to the circumstances, upon the great principles of justice and generosity, and in conformity with the wishes and welfare of the whole community. Among so many societies and associations as are organized under the general statute there will always be exceptional cases where, from their amount of business or other causes, they have come to exceed the limitation of capital allowed them, and it is reasonable that the state should have the privilege, if it pleases, of relaxing the statutory restraints in such exceptional cases. And the circumstances of the present case make the strongest appeal for the protection of this devisee against the loss of the generous gifts to it from one who loved the institution as he would have loved his child, and who devoted to its interests his time and services, and, as he supposed, a goodly share of his estate which had been earned by his industry and economy for a long lifetime. And it may not be amiss to state the fact that the legislature has lately increased the limitation of capital which the infirmary may hold from one hundred thousand to one million of dollars.

There is but little authority, either English or American, favoring the conclusion that bequests or devises not strictly authorized by law are to be considered void instead of voidable. This will be seen in the examination of cases in this country to be made in the progress of this discussion. But it may also be worth the while to notice what application has been made of the principle by the English courts in view of the statutes of mortmain as existing in that country. In *Grant on Corporations*, a reputable English work on the subject, at page *101, the author states the doctrine as follows: "The meaning of the term unlicensed corporation is this. As was

observed above, the conveyance of lands to a corporation was not made void to all intents and purposes by the statutes of mortmain, but only voidable at the option of the lords and the crown; consequently if the mesne lords and the crown all consented to waive the escheat, each in their respective rights, the corporation to whom the land was granted enjoyed the property unmolested. In process of time the rights of the lords becoming difficult to trace, a license from the crown was generally considered sufficient to ascertain the right of property to the corporation; and this license it became usual for corporations to obtain from the crown, enabling them to take lands to such a value, notwithstanding the statutes of mortmain. In strictness, however, the license to hold in mortmain was only waiver of the right of the crown to enter on the lands alienated; for as no royal charter can per se take away the property, or prejudice the interest of the subject, such license did not abrogate the right of the mesne lords to enter, and therefore, with respect to them, the corporation was not secure until the lapse of the periods respectively limited for the assertion of their rights. In fact the king's license had only the effect of waiving the crown's right to the escheat, etc., etc." The author further says: "The question is of the more importance, as there is no doubt that many corporations have greatly exceeded the limits of their license, and hold such surplus lands without any right derived from it for their doing so. It is clear, however, that if a corporation have exhausted their license to hold in mortmain, the fact does not make a devise or conveyance to them void. The only result is, that they may take, though, unless they can obtain an extension by the crown of their license, they cannot hold the lands, unless the mesne lords and the crown choose to sleep upon their respective titles."

The cases in this country, most of them which favor the principle that an estate in the condition this is goes to the heirs of a testator, rather than to the devisee, seem to inculcate the idea that the heirs may waive their right so as to allow the estate to pass to the devisee. And we have not the slightest doubt that, but for the interference of the heirs in the present case by this bill in equity, no obstacle would have stood in the way of a complete administration of the testator's estate according to his clearly expressed intention. No court would have had the least hesitation in following the ordinary course of procedure, or would have entertained the thought, *suo moto*, of instituting inquiry to see whether the bequests in question were valid or not. But why should a bequest, invalid when not consented to by the heirs, become unobjectionable when such consent is obtained? If illegal as coming from the testator, why not just as illegal when coming from the testator and his heirs? Such considerations as these go to show how illogical and untenable a position it is to denominate the devises and bequests in the present will absolutely void.

Each side relies on certain authorities in defense of its position,

and between the two sides many have been referred to. The first one relied on by the complainants, and probably one of the earliest decisions on the question in this country, is *Trustees of Davidson College v. Chamber's Executors*, reported, in 1857, in 3 Jones, N. C. Eq. 251. The same question arose there that exists here, and the case was decided according to the contention of the complainants in this case. It went on the theory that, as the college was seeking to obtain an illegal bequest, the law could not assist it to do so, and that the bequest was absolutely void. It was a severe and technical decision, reasoned out without the aid of authorities, as few in this country existed to throw light on the subject at that time. But the opinion admits that its severe doctrine did not apply to real estate and only to personal property. Should that be the law in this state, and we do not see why not if the law of that case is to prevail here, it may turn out that the residuary clause here is valid as operative only on real estate. But in our judgment the dissenting opinion in that case by NASH, C. J., is more satisfactory than the prevailing opinions delivered by the two associate justices. The argument of the chief justice is more in consonance with the doctrine which has grown up since that day. The chief justice, after declaring that the restriction as to amount of corporate property is merely directory, and that the bequest was not void but at the most voidable, goes on to say: "If the restriction is a condition, it is a condition subsequent, for a breach of which no action can be taken against a corporation but by the sovereign; and with the latter and its officials it is a matter of discretion whether a forfeiture will be enforced or not. To work a forfeiture of chartered privileges there must be something more than accidental negligence, excess of power, or mistake; there must be something wrong arising from wilful abuse or neglect. There is here no judicial forfeiture for none has been judicially pronounced. Granting that, by taking the whole of the property devised, the total amount would exceed in value what the corporation was entitled to possess, and thereby its charter might be forfeited, can the defendants (executors) or next of kin take advantage of the condition in these proceedings? A charter is a contract between the corporation and the sovereign. It is well settled that none but the parties and their privies can take advantage of a breach of a condition. Now neither Mr. Chambers (donor) nor his executors, nor his next of kin are any parties or privies to this contract. Upon what principle then is it that the executor can refuse his assent to this legacy to the college, or upon what principle can the next of kin claim it or any portion of it?" * * *

The complainants also rely very much on the Cornell University case, reported in 1888, under the title of *Matter of McGraw*, 111 N. Y. 66, a strongly stated case and in point here, excepting as the New York policy differs from the policy maintained elsewhere, and as the municipal law there differs from the statutes of other states and especially from the statutory system of our own state. It is

there held that such devises and bequests as these are absolutely and irrevocably void, and in this respect the case is not wholly consistent with the views expressed by the same court in the Chamberlain case already commented on, and is in great advance of any doctrine expressed in any previous case in that state. The result is reached by an interpretation "of the general statutes of the state relating to the organization and holding of property by corporations of the class of Cornell University as the same have been affected by the terms of the special charter granted to it." While in our own state we have no statute affecting the question outside of the terms of the corporate charter itself, or of the general law authorizing the charter, the New York code contains clauses touching the ability of corporations to acquire property which her court construes to be expressly and utterly prohibitory. The provisions are of themselves severe and they are also strictly and severely construed by the New York court. This same case came before the Supreme Court of the United States afterward, and that court declined to review the decision of the New York Court of Appeals upon the ground that no federal question was presented, inasmuch as the decision sought to be reviewed was based upon the charter of the university and the municipal law of the state of New York. *Cornell University v. Fiske*, 136 U. S. 152. The statute of wills in New York is disabling and restraining in its character and prohibits a devise to a corporation unless specially permitted by its charter or by some statute to take property by devise. Her statutes on analogous subjects have been restrictive and her decisions have been accordingly. Its code forbade a charitable trust to be created upon real estate. Its decisions decline to uphold a trust when a trust exists without a trustee, differing therein from the decisions of other states. Mr. Schouler (*Schoul. Wills*, § 26, note) says: "Under the policy of the New York code an unincorporated association appears to be treated with little favor as the beneficiary of a devise." The same restrictive policy led its highest court to hold that a mortgage to a national bank to secure future advances as well as past indebtedness was void (*Croker v. Whitney*, 71 N. Y. 161) and this doctrine was overruled by the more liberal policy of the United States Supreme Court in *National Bank v. Whitney*, 103 U. S. 99. * * *

The counsel rebel against regarding the National Bank cases as fitting precedents in support of the question here, but they are so regarded in some cases and by some authors, which shows how other minds than ours are influenced by them. So the counsel protest just as strongly against the alien cases as being of any importance as authority. But that class of cases is constantly cited in the books as supporting by analogy such a position as the respondents stand upon here. Deeds to aliens may not be of principal importance, but it seems to us that devises to aliens, which are good at common law, are clearly cases in point and of more consequence as precedents than any other analogous authority. Does not the will containing

a devise to an alien have to be approved with the same formalities as are required of the will of the present testator, and is the land devised any more in the possession of the devisee in the one case than in the other? It is argued in behalf of complainants that there is this distinction between an alien as devisee and a corporation as such; that in the case of an alien the disability is personal and does not attach until proved by some direct and not collateral proceeding, as bankruptcy must be proved in the case of a bankrupt or as felony must be proved in the case of a felon, before the full consequences of such a condition fall upon them. There must be a conviction. Is not that the very contention of the respondents here? What is there in this will which should lead a court to establish any illegality except by a direct proceeding for the purpose? And why should the law be any more generous to a bankrupt or a felon in the dispensation of its favors than to a charitable association? At common law, and by the statute law of some of the states, an alien can take real estate by devise and hold the same until office found to take it away from him. It is also argued for the complainants that executory contracts of an illegal nature where the illegality is participated in by both parties cannot be enforced by one party against the other, the parties being equally in fault. That principle is not applicable here. The executors and the corporation are not parties contending against each other. They are on the same side of this suit. It is admitted by the corporation that it would be a transgression of the law of its organization to accept the bequests unless the state actively or passively consents to it, and its silence is its consent. But what wrong has the testator committed by his act? The only contract that can be pertinently discussed here is that between the state and the corporation, and the state can do no wrong.

A few of the more important propositions pertinent to the case may, in conclusion, be briefly restated as these: That there is no restraining clause in our statute of wills preventing the testator from making these devises and bequests; that they are regular and valid on their face, nothing in the will indicating that the corporation might not be a competent trustee to administer the gifts; that the testator had no suspicion that there would be any question over the provisions of his will; that, if the bequests fail, it will be an accident caused by a mistake of the testator respecting a fact or as to the legal construction of such fact; that the same bequests (and devises) could have been safely made to almost any individual or to any one of many charitable corporations in the state instead of to this corporation; that there is a very narrow difference, if there be any, between selecting this institution and selecting any other suitable trustee for the execution of the trusts committed to it, such a corporation as this being merely a technical and metaphysical entity through which the benefit of the trusts were to go to poor persons suffering from certain diseases; that the heirs could have no voice or interest in the matter, unless accidentally so through the innocent mistake

of the testator, they having no lien on the estate of either a legal or moral kind; that there are no words in the charter of the corporation, or in the statute authorizing its organization, that forbid its holding more than the amount limited by the statute, nor any penalties attached whereby to punish any transgression of the limitation, the only punishment intended being the risk of a forfeiture of the bequests, or of the charter; that the limitation is chiefly directory and regulative, and; if impliedly prohibitory, incidentally and mildly so; that the charter is a contract between the corporation and the state in which no person is legally interested but the parties thereto, the same general rules of interpretation applying as in other contracts; that if the corporation fails to keep its side of the contract the state can take advantage of the default or not as it pleases; that the transgression may be so slight in its consequences that the state will forgive the offense, or forgive it because occasioned by some accident or error resulting while the corporation is acting in good faith, or the state may, acting through its prosecuting officers, punish the offense for the public good; that the state may by its legislature authorize the corporation to increase its capital before the act is done, or, if the increase be made without authority, may ratify the act afterward either by some legislative provision or, as may be done between any other contracting parties, by its silence and any other acts indicating consent; that from the foregoing propositions it is clearly deducible that bequests like the present are voidable only, and may be avoided by the state alone, and are in no sense to be regarded as void; that a policy arose as to what better be done in the circumstances of each particular case, and that that policy belongs to the state and not to the court and is an executive and *not* a judicial right, for the court would decide the question in the case for all cases and all time, while the state may decide the question differently at different times according to its discretion and the public good. This right the state has never surrendered and the court cannot take it from the state. But it would surely deprive the state of its privilege if the court fails to act upon these bequests as valid bequests until, in proper and independent proceedings, such bequests are declared to be void.

This conclusion renders it unnecessary and inexpedient to discuss the further contention of the respondents that the bequests are valid in equity if not at law, upon the maxim that no legal trust of a charitable nature shall fail for want of a competent trustee, and that if this corporation cannot act some other party may be appointed by the court that can.

Exceptions overruled.

Appeal dismissed, and decree below *affirmed*.⁸

⁸ *Hanson v. Little Sisters of the Poor* (1894) 79 Md. 434, 32 Atl. 1052 (bequest); *In re Stickney's Will* (1897) 85 Md. 79, 36 Atl. 654 (devise), *Accord.* *Matter of McGraw* (1888) 111 N. Y. 66, 19 N. E. 233; *Trustees of Davidson College v. Executors* (1857) 3 Jones Eq. (N. Car.) 253, *Contra.* In the last cited case, Battle, J., distinguishing between a bequest and a

WOOD v. HAMMOND.

1889. 16 R. I. 98, 17 Atl. 324, 18 Atl. 198.*

Bill for instructions by executors against all parties interested in the estate.

DURFEE, C. J. * * *

THE primary question is, whether a corporation, whose capacity to hold property is limited by its charter, can nevertheless take or hold as devisee or legatee in excess of the limit. There is some conflict of decision on this question. The doctrine of some of the cases is that the limit is operative only in favor of the state, and that as against all other persons the corporation can take and hold the same as if no limit were prescribed. The cases in which this doctrine has been declared have been for the most part cases where the corporations exceeding their limits have done so by purchase for value, and consequently where the vendor was estopped by his own conveyance from contesting the title conveyed, and equally so his heirs, or where the persons challenging the title were mere strangers to it, and as such in no position to question its validity. The doctrine, however, is laid down in *Jones v. Habersham*, 107 U. S. 174, 183, and in *De Camp v. Dobbins*, 29 N. J. Eq. 35, and in those two cases there was no estoppel, the property having been given by will. In each of them, however, the act imposing the limit had been altered or repealed before the will went into effect, so that the decision did not necessarily rest on the doctrine, and it would seem that the doctrine received only a cursory consideration. Moreover, *De Camp v. Dobbins* was reheard on appeal, and in the appellate court, though the decision of the court below was affirmed, Chief Justice Beasley, in delivering judgment, took occasion to disavow the doctrine very emphatically, giving reasons for the disavowal. See *De Camp v. Dobbins*, 31 N. J. Eq. 671, 690.

The doctrine of the three following cases is, that where property is given by will to a corporation, whose capacity to take or hold is limited by charter, or by the general statute law, the gift will be invalid in so far as it exceeds the limit, and to that extent will either go over under the will, or descend as intestate to the heirs or next kin of the testator. *Cromie's Heirs v. Louisville Orphans' Home Society*, 3 Bush, Ky., 365, decided A. D. 1867; *Chamberlain v. Chamberlain*, 43 N. Y. 424, decided A. D. 1871; *Matter of McGraw v. Cornell University*, 52 N. Y. Supreme Court, 354, decided A. D. 1887.

devise, said: "The devisee takes it (realty) at once by force of the will, and his title becomes complete immediately upon the death of the devisor. But the case of a legacy is well known to be different. * * * The legatee has no legal title to the legacy until the executor shall give his assent to it. * * * It needs the aid of a court, then, to enable the plaintiffs to recover this legacy which they claim."—Eds.

* Statement abridged. Only a portion of the opinion is given.—Eds.

In the first named case the gift was a residuary gift of real and personal estate, by the will of a citizen of Kentucky, to a charitable institution in New York, incorporated under a law of that state, by which it was authorized to take and hold real estate to an amount not exceeding \$50,000 in value, and personal estate to an amount not exceeding \$75,000 in value. The Court of Appeals of Kentucky, sitting in equity, decided that, inasmuch as it appeared that the institution had, when the testator died, real estate in excess of its limit, it should take no part of the real estate devised, and that it should take only so much of the personal estate bequeathed as should be required to carry its personal estate up to \$75,000, and that the whole of the real estate, and so much of the personal estate as should not be required as aforesaid, should go as intestate to the heirs and next of kin of the testator.

In *Chamberlain v. Chamberlain*, the gift was a residuary gift to an incorporated academy, authorized as such to take and hold, by gift, grant, or devise, real and personal property, the clear yearly income or revenue of which should not exceed the value of \$4,000, and the court held that it was not entitled to take as legatee beyond that limit. Said the court: "The institute can take and hold property within the limit prescribed, but can neither take nor hold in excess of that limit. Effect will not be given to a transgressive bequest in excess of the amount authorized. Claiming property and seeking the aid of the court to reach it, the corporation can rely only on the warrant and authority conferred by law, and cannot claim in transgression or excess of that authority. The statute permits the corporation to take property of a given yearly value, and prohibits the taking in excess of that value."

In *The Matter of McGraw*, the gift was a residuary gift of a very large property to Cornell University. The charter of Cornell University provided that "the corporation hereby created may hold real and personal property to an amount not exceeding three millions of dollars in the aggregate." The university had property to that amount when the testator died. The question was whether, notwithstanding this, it was entitled to take as legatee under the will in opposition to the claims of the heirs or next of kin. The Supreme Court decided, after careful consideration and on the authority of *Chamberlain v. Chamberlain*, that it could not. Thereupon the case was appealed to the Court of Appeals, where the judgment of the Supreme Court was affirmed. *Matter of McGraw*, 111 N. Y. 66. * * * It seems to us that the natural and logical conclusion, independently of authority, is, that an artificial body created by law, without capacity to take or hold property beyond a certain limit, cannot, by reason of the very law of its being, take or hold property beyond that limit, and consequently that the courts ought to recognize the fact in favor of any person who is entitled, on supposition of the incapacity of the corporation, unless by estoppel or otherwise such person is precluded from making claim. The contrary view seems to

have originated, partly at least, in the analogy which was supposed to exist between laws limiting corporate capacity in this respect and the old law of mortmain or the law of alienage. But the analogy, such as it is, is not close enough, as is clearly shown in the *Matter of McGraw*, to warrant such a view. The statutes of mortmain were so worded that they were construed, not to prohibit absolutely grants of land to corporations without license from the crown, but only to render such grants defeasible by the feudal superior of the grantor by entry for that purpose; and they were, in default of entry by any other feudal superior, forfeitable to the crown. And so, also, an alien might purchase land or take it by devise, but he would do so at the risk of having it forfeited to the crown upon inquest of office found. These old laws, founded on feudal reasons, throw little light on the meaning of modern statutes.

The provision in the charter of the Society for the Prevention of Cruelty to Children was not, as we have seen, that the society should not *take* property exceeding \$10,000 in value, but that it should not *hold* it, and it is contended that, under this language, it was competent for the society to take the property devised, and except as against the state, to hold it, and that, the state having enlarged its capacity, it can now hold it absolutely. The same argument was pressed with great ingenuity and in various forms in *The Matter of McGraw*, and the court, after patiently examining the argument in all its phases, held it to be unsound. The question is, of course, a question of legislative intent. It seems to us that the limitation on the power of the corporation to hold is necessarily an implied limitation on the power to take, for why take what it cannot hold? Indeed, the very act of taking involves an act of holding, momentarily at least. And, if the illustration be permissible, a vessel which is as full as it can *hold* is incapable of *taking* any more. And see *Bank of Michigan v. Niles*, 1 Dougl. Mich. 401.

We do not think the amendment of the charter, by which the capacity of the society to hold property was enlarged, is effectual to enable the society to take under the will in its larger capacity. The will, though the probate was not completed until after the amendment, took effect by relation, when proved, from the death of the testator, and became operative from that time, as if it was a special law of descent for the estate disposed of by it, and the rights of all persons, designated as devisees or legatees therein, are to be regarded as determined by it at that time, unless dependent on future contingencies. It follows that the property given to the society, beyond its capacity to hold, became immediately subject to the other dispositions of the will. * * *10

¹⁰ In *House of Mercy v. Davidson* (1897) 90 Tex. 529, 39 S. W. 924, *Accord*, *Brown, J.*, said: "Under the rule applied to purchase by an alien or corporation incapacitated to hold land, the vendor who has for a valuable consideration conveyed the property to such alien or corporation is estopped to deny the capacity of his vendee to take the title. The State alone can question such a title. But the doctrine of estoppel does not apply to a

HUBBARD v. WORCESTER ART MUSEUM.

1907. 194 Mass. 280, 80 N. E. 490.¹¹

KNOWLTON, C. J.—This is a petition brought by the heirs of Stephen Salisbury, late of Worcester, deceased, for leave to file an information in the nature of a *quo warranto* against the respondent, under the R. L. c. 192, §§ 6–13. The Worcester Art Museum is a corporation established under the provisions of the Pub. Sts. c. 115 (R. L. c. 125), “for the purpose,” as set forth in its certificate of incorporation, “of founding an institution for the promotion of art and art education in said Worcester; erecting and maintaining buildings for the preservation and exhibition of works and objects of art; making and exhibiting collections of such works, and providing instruction in the industrial, liberal, and fine arts; for holding real and personal estate in the furtherance of this purpose; and for the holding and administering funds acquired by the corporation for these and kindred objects in accordance with the will of the donors. All of said property and funds of the corporation, however, are to be held solely in trust for the benefit of all the people of the city of Worcester.” By the will of Mr. Salisbury this corporation is made his residuary legatee, and if the intention of the testator is carried out, it will receive, under the will, real and personal estate amounting in value to between \$2,000,000 and \$3,500,000. By the R. L. c. 125, § 8, such corporations are authorized to “hold real and personal estate to an amount not exceeding one million five hundred thousand dollars.” By the St. 1906, c. 312, enacted after the probate of the will, the right of this respondent to hold real and personal estate was enlarged to an amount not exceeding \$5,000,000. The petitioners contend that, by reason of the limitation in the statute, the gift was void; that, as heirs at law of the testator, their rights in this part of his estate became vested on the probate of the will; that the St. 1906 is prospective in its operation, and does not affect the right of the respondent to hold property under this will, and that, if it were construed as applying to property devised by this will, it would be unconstitutional and void.

The statute under which the petition is brought has been considered in *Goddard v. Smithett*, 3 Gray 116, in *Hartnett v. Plumbers' Supply Association*, 169 Mass. 229, and in other cases. We will assume in favor of the petitioners, without deciding, that if they were right in their view of the questions of substantive law involved, it would be available to give them the remedy which they seek. We come directly to the effect of the residuary clause in the will.

The attack upon its validity may be considered from two points of view: first, in reference to the rights of testators, as against their

testator, and if the devise named in a will has not the capacity to take the property the devise will be void and the law will vest the title in the heir.”—Eds.

¹¹ Portion of opinion omitted.—Eds.

heirs, to dispose of their property for charitable or other purposes; secondly, in reference to the provisions of the law giving this kind of corporations a right to hold property to an amount not exceeding a certain sum.

From the first point of view this gift is perfect and complete. Except for the protection of the statutory rights of a husband or wife, the power of a testator in this commonwealth to dispose of his estate by a will is unlimited. There is nothing in our law to restrain one from giving free course to his charitable inclinations, up to the last moment of his possession of a sound, disposing mind. Making charitable gifts in this commonwealth is not against public policy, and we have no legislation, such as has long existed in England and in New York and some of the other American states, putting obstacles in the way of testamentary acts. The only ground of objection to this part of the will is not from the point of view of the testator or of his heirs, but on account of the provision of the statute regulating the rights of corporations as to the holding of property. We must, therefore, determine the meaning and effect of this statute on which the petitioners rely.

They contend that it is by implication an absolute prohibition against the holding, at any time, in any form, for any purpose, of a greater amount of property than that stated, and that any attempt of a corporation to hold more, or of any person to put more into the ownership of a corporation, is illegal and absolutely void. The respondent contends that this implied limitation of the right to hold is made on grounds of public policy; that it is a provision only in favor of the state, which the state may enforce or not, as it chooses; that grants or devises in excess of the amounts stated are not void, but only voidable; that third persons cannot question the validity of such grants or devises, but that they are legal so long as the state leaves them undisturbed, and that the state may at any time, by a legislative act or in some other proper way, completely waive its right of enforcement.

In interpreting the act the history of earlier kindred provisions may be helpful. At common law, corporations were authorized to acquire and hold both real and personal property without limit. In *re McGraw's Estate*, 111 N. Y. 66, 84. "The creation of a corporation gives to it, amongst other powers, as incident to its existence, and without any express grant of such powers, that of buying and selling." *Bank v. Poitiaux*, 3 Rand. 136. "A corporation has, from its nature, a right to purchase lands, though the charter contains no license to that purpose." *Leazure v. Hillegas*, 7 S. & R. 313. See also *Page v. Heineberg*, 40 Vt. 81; *Mallett v. Simpson*, 94 N. C. 37, 41.

Under the feudal system, when land was given to a corporation, the chief lords of whom the land was held, and the king as ultimate chief lord, lost their chances of escheat, and various other rights and incidents of military tenure. During the middle ages, the accumula-

tion of land in the ecclesiastical corporations was so great as to be thought a national grievance. Hence the English mortmain acts, which go back for their origin to Magna Charta, St. 9 Hen. III, c. 36, and which have continued with various modifications to this day. See 7 Edw. I, c. 2; 15 Rich. II, c. 5; Shelford on Mortmain, 2, 6, 8, 16, 25, 34, 39, 809, 812; Tyssen on Charitable Bequests, 2, 383. Under these acts the alienations were not void, so as to let in the grantors and their heirs; but they merely operated as a forfeiture, which gave a right to the mesne lord and the king to enter after due inquest. This right to enter was often waived by a license in mortmain. See citations above, and Tyssen on Charitable Bequests, 383; St. 7 & 8 Will. III, c. 37. In form these licenses commonly authorized a holding of property "not exceeding" a certain value. In later years this authority sometimes has been inserted in the charter, and this limited power of purchase has, it is said, been exceeded by almost all corporations. Shelford on Mortmain, 55. See also pages 10, 44, 49, 56, 891; Tyssen on Charitable Bequests, 393, 394, 396.

Another act, St. 9 Geo. II, c. 36, which is usually called "The Mortmain Act," but is called by Tyssen the "Georgian Mortmain Act," is of a very different nature. One of its purposes, as declared in the preamble, is to avoid "improvident alienations or dispositions made by languishing or dying persons, or by other persons, to uses called charitable uses, to take place after their deaths, to the disherison of their lawful heirs." Considered in reference to its purposes, it is not properly called a mortmain act. It applies only to gifts for charitable uses; and under it all such gifts, unless made as the statute allows, are absolutely void.

We never have had any real mortmain acts in Massachusetts. The nearest approach to one was the Prov. St. 1754-55, c. 12; 3 Prov. Laws (State ed.) 778. This made deacons a corporation to take gifts for charitable purposes, limited the grants to such as would produce an income not exceeding three hundred pounds a year, and provided that they should be made by deed, three months before death, and that all bequests, devises, or later grants should be void. This statute related only to gifts to deacons, and was repealed by St. 1785, c. 51 (February 20, 1786), which reenacted a part of the law, but omitted the provision that gifts not authorized by the act should be void. *Bartlet v. King*, 12 Mass. 537, 545. See R. L. c. 37, § 1.

The significance of this reference to English law and to our legislation is, first, that, except for this short period, we have never had in Massachusetts any legislation prohibiting charitable gifts to trustees or corporations, or providing that any kind of conveyances, devises, or bequests to corporations shall be void. On the other hand, the policy of the commonwealth, as expressed both by legislation and the decisions of its courts, has been exceedingly liberal to testators and public charities. *Sanderson v. White*, 18 Pick. 328, 333, 334; *American Academy v. Harvard College*, 12 Gray 582, 595, 596; *Sal-*

tonstall v. Sanders, 11 Allen 446; Jackson v. Phillips, 14 Allen 539, 550. Secondly, the implied limitations upon the power of corporations to hold property, which appear in numerous enactments, have been made, not in the interest of grantors or devisors or their heirs, but in the interest of the state, on considerations of public policy. The general form of these limitations, which appears in the statute before us, and with slight variations in special charters (a list of which, two hundred and seventy-four in number, granted in this state before 1850, has been furnished us through the industry of counsel) corresponds with the form of licenses granted by the Crown in England under the old mortmain acts, and sometimes embodied in charters granted by parliament. Under these English acts, grants or devises to a corporation to hold property without a license, or in excess of the amount licensed, were not void, but only voidable by the mesne lord or the king, upon entry, after inquest according to law. In view of the close relations between Massachusetts and the mother country in early times, this justifies an argument, of considerable strength, that the implied limitations in our statutes were intended to have no greater force than the old mortmain acts of England, as distinguished from the Georgian mortmain act.

We start with the inherent right, already referred to, of every corporation to take and hold property at common law, by virtue of the act of its creation. This right is recognized in our statutes by implication, without express mention. R. L. c. 109 §§ 4-6. What force is to be given to the words, "may hold real and personal estate to an amount not exceeding one million five hundred thousand dollars"? The respondent contends that their meaning is as if words were added as follows: "and beyond that amount it shall have no right as against the commonwealth; and the commonwealth may take proper measures, through action of the attorney-general or otherwise, to prevent or terminate such larger holding." According to the argument, a taking and holding by a corporation, above the prescribed amount, is under its inherent right. As between it and the state as the guardian of the public interest, a provision as to amount is made, which does not affect its right as to third persons. As to the general legality of the holding, except when the state chooses to enforce the law for its own benefit, the condition is similar to that resulting from a statutory provision which is merely directory. It is not very unlike the old law as to conveyances to aliens. Such conveyances, whether by grant or devise, were good against every one but the state, and could be set aside only after office found. Fox v. Southack, 12 Mass. 143; Waugh v. Riley, 8 Met. 290; Judd v. Lawrence, 1 Cush. 531; Kershaw v. Kelsey, 100 Mass. 561.

That this is the effect of such limitations in statutes of this kind where the title of the corporation is under a grant, as distinguished from a devise, seems to be the universal rule. Vidal v. Girard, 2 How. 127, 191; Runyan v. Coster, 14 Pet. 122; National Bank v. Matthews, 98 U. S. 621; Cowell v. Springs Co., 100 U. S. 55, 60;

Jones v. Guaranty & Indemnity Co., 101 U. S. 622; National Bank v. Whitney, 103 U. S. 99; Fritts v. Palmer, 132 U. S. 282; Leazure v. Hillegas, 7 S. & R. 313; Chambers v. St. Louis, 29 Mo. 543; Bank v. Poitiaux, 3 Rand. (Va.) 136; Fayette Land Co. v. Louisville & Nashville Railroad, 93 Va. 274; Mallett v. Simpson, 94 N. C. 37; Gilbert v. Hole, 2 So. Dak. 164; Barrow v. Nashville & Charlotte Turnpike Co., 9 Humph. 304; Hough v. Cook County Land Co., 73 Ill. 23; Alexander v. Tolleston Club, 110 Ill. 65; Barnes v. Suddard, 117 Ill. 237; Hamsher v. Hamsher, 132 Ill. 273; Baker v. Neff, 73 Ind. 68, 70. This is a fair deduction from the decisions in this commonwealth. Heard v. Talbot, 7 Gray 113; Commonwealth v. Wilder, 127 Mass. 1, 6; Davis v. Old Colony Railroad, 131 Mass. 258, 273; West Springfield v. West Springfield Aqueduct Co., 167 Mass. 128; Slater Woollen Co. v. Lamb, 143 Mass. 420; Prescott National Bank v. Butler, 157 Mass. 548; Nantasket Beach Steamboat Co. v. Shea, 182 Mass. 147; National Pemberton Bank v. Porter, 125 Mass. 333; Atlas National Bank v. Savery, 127 Mass. 75; Bowditch v. New England Ins. Co., 141 Mass. 292; Chaffee v. Middlesex Railroad, 146 Mass. 224.

The counsel for one of the petitioners says in his brief, "It is fully conceded at the outset that where a corporation takes and holds property by conveyance, or by executed gift *inter vivos*, contrary to its charter rights, no one but the state can complain. This is settled by a practically unbroken line of decisions in all the states," etc.

But if the statute were a prohibition that renders the holding utterly void, and the taking also void, as is argued in the opinion in *In re McGraw's estate*, 111 N. Y. 66, anybody interested could take advantage of the violation of law, unless he was precluded by estoppel. Most of the cases which we have cited do not put their decision on the ground of estoppel. Often the question might arise when there was no estoppel. The ground on which most of the cases go is that the implication is not an absolute prohibition, but only a condition affecting the rights of the corporation as between it and the state. If the holding were an illegality which was utterly void, the condition would be the same whether the taking was by grant or devise, and a variety of unfortunate consequences might follow. The property might greatly increase in value after its acquisition, as was the case in *Evangelical Baptist Society v. Boston*, 192 Mass. 412. In that case, although the property of the corporation largely exceeded in value the amount authorized by the statute, there was no intimation that the holding was illegal, so long as the state did not interfere. See also *Humbert v. Trinity Church*, 24 Wend. 587, 605. As to all interests of private persons, in the absence of interference by the state, the cases generally treat titles to property held by corporations in excess of the specially authorized amounts as good. They allow the corporations to give good titles to purchasers of such property.

Some judges, in holding that such titles cannot be taken under wills, endeavor to found a distinction upon the executed character of

a title by grant, and suggest that a devise or bequest is executory. It seems to us that there is no good reason for the distinction. When a will is proved and allowed, it takes effect immediately to pass all property affected by it. The provision in the law against large holdings by corporations has no relation to the probate of the will. The act of the testator in executing the will is confirmed and given effect as a complete and executed disposition of the property, by the allowance of the will. In this respect a recorded will does not materially differ from a delivered deed. The heirs at law are bound by one as well as by the other.

The decisions upon the precise point at issue are conflicting. In *Jones v. Habersham*, 107 U. S. 174, a case similar to that now before us, it was held by the court, in an opinion by Mr. Justice Gray, that "restrictions imposed by the charter of a corporation upon the amount of property that it may hold, cannot be taken advantage of collaterally by private persons." In the same case in the circuit court the question had been considered previously, and the same result was reached, in an opinion by Mr. Justice Bradley of the Supreme Court of the United States, which is found in 3 Woods 443, 475. The same rule is established in Maryland. *Hanson v. Little Sisters of the Poor*, 79 Md. 434; *In re Stickney's will*, 85 Md. 79, 104. *DeCamp v. Dobbins*, 2 Stew. (N. J.) 36, 40, was decided by the chancellor on this ground. The decree was affirmed on another ground in the Court of Errors and Appeals, 4 Stew. (N. J.) 671, 690, in an opinion by Beasley, C. J., which contains a dictum disapproving of the view of the chancellor. In *Farrington v. Putnam*, 90 Maine 405, the court, in a very elaborate opinion, in a case identical in its leading features with that now before us, held that the gift was good. The same doctrine is stated in *Brigham v. Peter Bent Brigham Hospital*, 126 Fed. Rep. 796, 801; s. c., 134 Fed. Rep. 513, 527. It is also stated in text books. *Beach, Corp.* (Purdy's ed.), § 825; *Thompson, Corp.* §§ 5795, 5797.

The leading case which presents the opposite view is *In re McGraw's estate*, 111 N. Y. 66. Although the decision necessarily puts a construction upon a statute of that state, this construction seems to be materially affected by the policy of New York in reference to charities. Said Judge Peckham, who delivered the opinion, "We have a decided mortmain policy. It is found in our statute in relation to wills, prohibiting a devise to a corporation unless specially permitted by its charter or by some statute to take property by devise." In *Chamberlain v. Chamberlain*, 43 N. Y. 424, the court refers to the prohibition of devises, and to the N. Y. St. 1860, c. 360, still in force, which makes void all bequests or devises to charity in excess of one-half the testator's property, where he leaves relatives. Other statutes have been passed, limiting the amount that can be devised to certain corporations by one testator, forbidding a devise or bequest to charities, by a person leaving relatives, of more than one-fourth of his estate, and making void such gifts where the will was executed

within two months before the death of the testator. Gen. Laws of N. Y. 1901 (Heyd. ed.), 4885, 4891, 4892. The policy of that state in regard to charities has been very unfavorable. See *Allen v. Stevens*, 161 N. Y. 122, 139, 140; *People v. Powers*, 147 N. Y. 104; *Fosdick v. Hempstead*, 125 N. Y. 581.

The doctrine of the New York court is stated as the law in *Davidson College v. Chambers*, 3 Jones Eq. 253, and adopted in *Wood v. Hammond*, 16 R. I. 98, 115, and *House of Mercy v. Davidson*, 90 Tex. 529. In the case in North Carolina the decision was by two of the three judges of the court, the chief justice giving an able dissenting opinion. The courts in Kentucky and Tennessee have expressed approval of the McGraw case in New York, but in terms that do not leave the grounds of their decisions entirely clear. *Cromie v. Louisville Orphans' Home Society*, 3 Bush 365, 383; *Heiskell v. Chickasaw Lodge*, 87 Tenn. 668, 686. In reference to supposed errors in the opinion in the last case, see *Pritchard on Wills*, § 153, note, and *Farrington v. Putnam*, 90 Maine 405, 433.

In the construction of our statute, when the question arises whether a different rule shall be established in regard to the taking and holding by a corporation under a will from that which is universally laid down in regard to a holding under a deed, we are much influenced by the policy of our law as to devises and bequests for charitable purposes. We are of opinion that, under the R. L. c. 125, § 8, a gift to a corporation under a will, to an amount in excess of the sum specially authorized, should be held no less valid than a similar acquisition of title under a deed. It is good as against every one but the commonwealth. It follows that the St. 1906, c. 312, operated as a waiver of the commonwealth's right to terminate the holding, and a legislative declaration of the entire validity of the provision in the will.

If we are wrong in this conclusion, the petition must be dismissed on an independent ground. (The learned judge proceeded to hold that the gift could also be sustained as a gift to a public charity.)

*Petition dismissed.*¹²

Section 2.—Ultra Vires Transfer of Property.

FAIRTITLE v. GILBERT.

1787. 2 Term Rep. (D. & E.) 169.

THE defendants were nominated trustees under the 11th Geo. 3, c. 87, for repairing and widening the road between Cheadle and Leek, in the county of Stafford, and for other purposes therein men-

¹² *Evangelical etc. Missionary Society v. City of Boston* (1910) 204 Mass. 28, 90 N. E. 572; *Jones v. Habersham* (1882) 107 U. S. 174, 27 L. ed. 401. 2 Sup. Ct. 336; *Brigham v. Peter Bent Brigham Hospital* (1903) 126 Fed.

tioned. The trustees are authorized by the act to erect turnpikes and toll-houses; and the right and property thereof, and all the materials of the same, are thereby vested in them. And seven or more of them are enabled by writing under their hands and seals to lease the said tolls. And they are further authorized to take up at interest any sum upon the credit of the said tolls, and to assign over and convey the said respective tolls to any person who shall advance their money thereon. It is further enacted, that no preference shall be given to the person lending money on the credit of the said tolls, in respect of the priority of advancing such sum; but that all persons to whom such respective mortgages or assignments shall be made, shall be in their several proportions creditors on the said respective tolls in equal degree one with another; and this is to be deemed a public act. The trustees having occasion to raise a certain sum, advertised according to the act, and the lessors of the plaintiff having offered to supply them, mortgages were executed to the lessors of the plaintiff of the tolls, and also of the toll-houses and toll-gates, by a sufficient number of the trustees, some of these very defendants having joined in executing those conveyances. This ejectment was brought to recover possession of the toll-houses and toll-gates, pursuant to the terms of the mortgage to Mytton. At the trial before Perryn, B., at the last assizes at Stafford, it was objected on behalf of the defendants, that the act did not warrant them to mortgage the toll-gates, but only the tolls, for which an ejectment would not lie; and that the act expressly directed that no preference should be given to any of the creditors above the rest; and the judge being of that opinion, non-suited the plaintiff.

ASHHURST, J.—It is clear that the trustees under this act of parliament had no power to mortgage the toll-houses or the turnpike-gates. The act expressly gives the trustees power to mortgage the tolls; but the reason why it does not give them a farther power is because no creditor is to have a preference. Now if any creditor had a power to enter and take possession of the toll-gates, he would gain a priority which the act has denied. And it is very fit that this should not be taken out of the hands of the trustees; because they are trustees for all the creditors, and were considered by the legislature as the most proper persons to have the whole management of everything to be done in pursuance of the act. It was foreseen that the whole sum wanted would not be advanced by any one person; and therefore, for the encouragement and security of all persons who were willing to advance money, it was necessary that the collection of the tolls should remain with the trustees. As then the trustees had no power to mortgage the toll-houses, the next question is, whether they are estopped to say so? In general the party granting is estopped by his deed to say he had no interest; but that general principle does not

796, affd. (1904) 134 Fed. 513, 67 C. C. A. 393; *Hubbard v. Worcester Art Museum* (1910) 179 Fed. 406, *Accord*. See also *McCartee v. Orphan Asylum Society* (1827) 9 Cow. (N. Y.) 437.—Eds.

apply to this case, where the trustees were not acting for their own benefit, but for the benefit of the public; and it would be hard that other creditors who are not parties to the deed, should lose the benefit which the act has given them. Besides, there is a still farther reason why the trustees should not be estopped; for this is a public act of parliament, and the court are bound to take notice that the trustees under this act had no power to mortgage the toll-houses. This deed therefore cannot operate in direct opposition to an act of parliament, which negatives the estoppel.

BULLER, J., and GROSE, J., of the same opinion.

*Rule discharged.*¹

COMMONWEALTH v. SMITH.

1865. 10 Allen (92 Mass.) 448.²

BILL IN EQUITY seeking to impeach the validity of a mortgage, executed on the 30th of July, 1855, by the Troy and Greenfield Railroad Company to the defendants as trustees, covering by its terms the franchise, railroad and all other property of the corporation, then owned or thereafter to be acquired, to secure bonds to the amount of \$900,000, to be issued to the contractor as part compensation for constructing the railroad, payable in thirty years from date. This mortgage recited the provisions of a contract for the construction of the railroad, dated December 30, 1854, to the effect that such bond should be given; and it was made subject to a prior mortgage to the Commonwealth, to secure state bonds to the amount of \$2,000,000, which the Commonwealth were to issue under the provisions of St. 1854, c. 226.

The following facts were agreed: Since the execution of the mortgage to the defendants, the Commonwealth have received two other mortgages upon the railroad and franchise of the Troy and Greenfield Railroad Company, one of which was dated on the 6th of July, 1860, and the other on the 5th of March, 1862; and also a surrender from the corporation of all their property, subject to redemption under St. 1862, c. 156. On the 4th of September, 1862, the Commonwealth took possession of the mortgaged premises in various towns, for breach of condition, in the manner shown by various certificates thereof, which are now immaterial. The Commonwealth under their various mortgages have at various times, from October, 1858, to July, 1861, advanced to the Troy and Greenfield Railroad Company large sums of money, amounting in all to several hundred thousand dollars. The corporation, under their mortgage to the defendants, have at various times, from August, 1855, to July, 1861, issued bonds

¹ See also *Doe ex dem. Banks v. Booth* (1800) 2 Bos. & P. 219.—Eds.

² Statement abridged. Portion of opinion omitted.—Eds.

to the amount in all of \$600,000, payable in thirty years from date. All of these bonds were issued in good faith, and are held by bona fide holders, and the corporation have issued no other bonds than the above.

HOAR, J.—The question whether the mortgage made to the defendants by the Troy and Greenfield Railroad Company is of any validity against the Commonwealth requires the court to give a construction to the provisions of St. 1854, c. 286. To ascertain what the legislature intended to authorize or prohibit by that statute, it will be expedient first to consider what were the powers of railroad companies in relation to the issue of bonds and the making of mortgages at common law, or before the statute was enacted.

There seems to be no reason why a railroad corporation should not be considered as having power to make a bond for any purpose for which it may lawfully contract a debt, without any special authority to that effect, unless restrained by some restriction, express or implied, in its charter, or in some other legislative act. A bond is merely an obligation under seal. A corporation having the capacity to sue and be sued, the right to make contracts, under which it may incur debts, and the right to make and use a common seal, a contract under seal is not only within the scope of its powers, but was originally the usual and peculiarly appropriate form of corporate agreement. The general power to dispose of and alienate its property is also incidental to every corporation not restricted in this respect by express legislation, or by "the purposes for which it is created, and the nature of the duties and liabilities imposed by its charter." *Treadwell v. Salisbury Manuf. Co.*, 7 Gray 404.

But in the case of a railroad company, created for the express and sole purpose of constructing, owning and managing a railroad; authorized to take land for this public purpose under the right of eminent domain; whose powers are to be exercised by officers expressly designated by statute; having public duties, the discharge of which is the leading object of its creation; required to make returns to the legislature; there are certainly great, and, in our opinion, insuperable objections to the doctrine that its franchise can be alienated, and its powers and privileges conferred by its own act upon another person or body, without authority other than that derived from the fact of its own incorporation. The franchise to be a corporation clearly cannot be transferred by any corporate body, of its own will. Such a franchise is not, in its own nature, transmissible. The power to mortgage can only be coextensive with the power to alienate absolutely, because every mortgage may become an absolute conveyance by foreclosure. And although the franchise to exist as a corporation is distinguishable from the franchises to be enjoyed and used by the corporation after its creation, yet the transfer of the latter differs essentially from the mere alienation of ordinary corporate property. The right of a railroad company to continue in being depends upon the performance of its public duties. Having once established its

road, if that and its franchise of managing, using and taking tolls or fares upon the same are alienated, its whole power to perform its most important functions is at an end. A manufacturing company may sell its mill, and buy another; but a railroad company cannot make a new railroad at its pleasure.

The whole reasoning of the court in the case of *Whittenton Mills v. Upton*, 10 Gray 582, in which it was held that a manufacturing corporation has no power to make a contract of co-partnership, applies with much greater force to the transfer of its franchise by a railroad company.

No case has been cited in which the exercise of such a power has ever been judicially sanctioned in this commonwealth, where there was not express legislative authority for it; and the cases in which the legislature has expressly conferred the power, or confirmed its exercise, furnish at once a strong implication that it would not otherwise exist, and afford a solution of the allusion to railroad mortgages which occurs in the statutes.

(The court *held* that the statute likewise did not permit the issue of the bonds and mortgage in question held by defendants, and that both were invalid.)

We find no evidence that the Commonwealth has ever known and sanctioned the irregular and illegal issue of the bonds in question, either directly or by implication. Nor do we think that they fall within the class of cases in which it has been held that a violation of corporate powers cannot be taken advantage of collaterally. The second mortgage to the Commonwealth gives it a direct interest in the property, and, not being made expressly subject to any prior incumbrance, gives the right to maintain and prove that the supposed conveyance to the defendants was illegal and void.

The result to which the point decided leads is this: that, the defendants having no title which they can maintain against either of the mortgages to the Commonwealth, the plaintiffs have a plain, complete and adequate remedy at law for any interference with the mortgaged property, and the bill must be dismissed.

MADISON AVENUE BAP. CHURCH v. BAPTIST CHURCH
IN OLIVER STREET.

1878. 73 N. Y. 82.*

APPEAL by both parties from judgment of the general term of the superior court of the city of New York, affirming a judgment, entered upon a decision of the court at special term. (The decision upon a former appeal is reported in 46 N. Y. 131.) (Reported below, 9 J. & S. 369.)

* Portion of opinion omitted.—Eds.

This was an action of ejectment, commenced July 30, 1863, to recover possession of certain real estate situate upon Madison avenue, in the city of New York, with a church edifice thereon.

The answer alleged in substance that the defendant entered into possession of the premises in October, 1862, under a deed from the plaintiff, executed in pursuance of an order of the Supreme Court, upon the plaintiff's petition. The petition and deed were the result of a plan of union previously adopted by the two corporations parties hereto, which provided for the extinction of the plaintiff's corporation, the surrender of all its property to the defendant, the transfer of its name and of all its members to the defendant's society. The answer set forth the plan of union, the petition, the Supreme Court order, and conveyance under it, possession under the deed with plaintiff's consent, and claimed the fee thereunder, and that its possession be confirmed. It also alleged payment by defendant of plaintiff's debts to the amount of \$16,154.23, and purchase by and assignment to it of a bond and mortgage given by plaintiff for \$12,500; also claimed the rights of mortgagee in possession, under said mortgage, and foreclosure in case its title in fee was not sustained, and also reimbursement for the moneys paid by the defendant on plaintiff's account while in possession. The petition signed by the plaintiff's trustees stated in substance that the plaintiff was the owner of the lots in question, and had erected a church edifice thereon, the whole costing \$122,000. That their present indebtedness was \$73,000, sixty-one of which was secured by mortgages upon the property. That from various causes stated in the petition it was unable to pay its liabilities or meet the current expenses of the church. That the plaintiff and defendant (a religious corporation under the laws of the state, located in Oliver street, and which for some time had contemplated disposing of its property, and moving up-town), had formed a plan and made arrangements for uniting the two churches upon the following terms: That the plaintiff should convey all its property to the defendant, and that the members of the Madison Avenue Baptist Church were to become, and be members, of the Oliver Street Baptist Church, and thereupon the regular services of the united churches were to be held in the house of worship then owned by the plaintiff. That the trustees of the defendant were to resign, and a new election of trustees had by the united church and congregation. That thereupon the defendant was to take the corporate name of the plaintiff. That the real and personal property of both was to become liable for the indebtedness of both. An agreement for disposing of the pews in the edifice of the plaintiff after the union was consummated. That the plan of union had been agreed to by both corporate bodies. That the defendant owned property over and above its indebtedness of the value of from \$50,000 to \$65,000, which, upon the consummation of the union, would become applicable to the payment of the debts of the plaintiff, and that by the union the creditors of the plaintiff would obtain that amount of additional security for the pay-

ment of their debts. That the two churches had obtained subscriptions for about \$15,000, to be applied to the payment of the floating indebtedness of each. Then follows a statement of a number of pew holders and pew hirers concurring in the application, that the others favor it, and that the rights of pew owners and holders will be protected.

Defendant put in a supplemental answer setting forth the purchase by and assignment to it, October 17, 1863, of another bond and mortgage, executed by plaintiff, of \$30,000, the whole of which was due, and averred that defendant was lawfully in possession of the premises under said mortgage. It alleged, also, that it held, as assignee, certain bonds then due, executed by plaintiff, secured by a trust mortgage on the premises, and alleged payment of other debts of plaintiff, not set forth in the answer, to the amount of \$2,224.18. Judgment of foreclosure upon the \$30,000 was demanded.

Plaintiff put in a supplemental complaint, claiming that if it should be adjudged that defendant acquired any right of foreclosure or of possession under the mortgages, or any right of lien for the reimbursement of sums paid out on account of plaintiff's debts, that an account should be taken of rents and profits, and defendant should be charged therewith, and be adjudged to surrender the premises upon being paid the balance, if any. The further facts appear sufficiently in the opinion.

EARL, J.—Upon the prior appeal in this case to this court it was decided that the Supreme Court had no jurisdiction to grant the order authorizing the conveyance by the plaintiff of its church property to the defendant, and hence that such conveyance was invalid. It was held that the court could authorize a conveyance only in the case of a sale, and that the facts did not show a sale. It was also held that by the common law in force in this state, religious corporations were restrained from alienating their real estate, and that when the conveyance now in question was made they could alienate their real estate only when authorized by the court, under section 11 of the act "to provide for the incorporation of religious societies," passed April 5, 1813, or when authorized by some act of the legislaturé. (*Madison Ave. Baptist Church v. Baptist Church in Oliver Street*, 46 N. Y. 131.) The case, so far as concerns the sale and conveyance, is the same now in all its essential features as it was before. The jurisdiction of the Supreme Court to make the order authorizing the conveyance depended upon the facts before it when it made the order. Its jurisdiction cannot now be upheld by showing that facts existed which were in no way placed before it, or brought to its attention or considered by it. The Supreme Court based its action entirely upon the petition presented to it by the plaintiff, and the only facts it considered were such as were alleged in that petition, and it was decided that those facts did not give the court jurisdiction to make the order. But if every fact which actually existed had been brought to the attention of the court at the time the order

was made, ~~it~~ still would not within the prior decision of this court have had jurisdiction to grant the order for the simple reason that all the facts do not show a sale within the meaning of section 11. The whole scheme was to effect a union of the two churches. The defendant was to absorb all plaintiff's property, assume its debts and take its corporate name and all its corporators and the congregation worshipping in its church. No price was agreed upon, as the value of plaintiff's property, which defendant was to pay. The plaintiff was to be dissolved as a corporation, and was to reap no benefit from the conveyance. On the contrary, the conveyance was intended to work its destruction. The defendant was to pay plaintiff's debts, which was mostly a lien upon its property, not for plaintiff's benefit, but for its own benefit. The plaintiff, which was at once to die, could not be benefited by the scheme.

It is argued with much zeal on the part of the defendant that, although the conveyance was *ultra vires*, yet, as it had been executed, and the whole arrangement connected therewith had been consummated, it must be permitted to stand. But this point was necessarily involved in the prior appeal to this court, and must have been decided adversely to the defendant. It would nullify the restraining law if the conveyance of a religious corporation could be held valid, because it had executed and delivered its deed, and received the consideration therefor. Corporations may incur responsibilities by acts which are *ultra vires*. But contracts, which they are prohibited from making, whether executory or executed, cannot be held valid. They may sometimes be estopped from asserting the invalidity of such contracts, and thus be practically bound by them. But that is not because the contracts are valid, but because it would be fraud upon the other party to assert their invalidity. (Bissell v. Mich. So. R. R., 22 N. Y. 258.)

It was, therefore, properly held in the court below, following the prior decision of this court, that the Supreme Court had no jurisdiction to grant the order authorizing the conveyance, and that the title to the property remained in the plaintiff. It remains to be considered whether the rights and obligations of the parties connected with, and dependent upon, the conveyance and transfer of possession of the property to the defendant were properly adjudicated in the court below. In 1862, at the time of the proposed union of the two churches, the plaintiff owned a church in Madison avenue, fully completed and equipped; but it was financially embarrassed, and unable to meet its current expenses. It was largely in debt, and the value of real estate at that time was greatly depressed. Its property had cost about \$122,000. Its debts were at least \$73,000; of which \$61,500 were secured by mortgages upon its real estate. The defendant at the same time owned a church in Oliver street, and real estate in other parts of the city worth upwards of \$75,000, and it owed nearly \$16,000, of which \$7,000 were secured by mortgage upon its real estate. Its members desired to secure a place of wor-

Delis
lower
stand.

?

ship in a more desirable quarter of the city, and negotiations for a union with plaintiff were entered upon, and a scheme for the union was devised and agreed upon by plaintiff and defendant, of which the following were the principal features:

The plaintiff was to transfer and convey to the defendant all its real and personal property, and was then to be dissolved. It was to make out a list of its members duly certified by its clerk, and such members were to be received as members of the defendant. The trustees of the defendant were to resign, and six new trustees were to be elected, three from the former members of the plaintiff, and three from the former members of the defendant. The defendant was to have its name changed to that of the plaintiff, and the property of both corporations was to be liable for the debts of both. After such election of trustees there was to be a sale of the pews in the Madison avenue church, and regular religious services were to be conducted by the defendant in that church. This scheme was substantially carried out. The plaintiff under the order of the Supreme Court conveyed its property to the defendant, and the defendant, by an instrument in writing, agreed to assume and pay all plaintiff's debts. All the plaintiff's members were admitted to membership in defendant's church. Defendant's trustees resigned, and six trustees were elected in their places, as provided in the scheme; and there was a sale of the pews and change of defendant's name, as also provided. The defendant sold its property, and realized therefrom, over and above the incumbrance thereon, the sum of \$68,400.10. It was one of the conditions upon which the union was to be consummated that both churches should raise by voluntary subscriptions sufficient money to pay off the floating debts of both. Accordingly such subscriptions were made, and the floating debts of both churches were paid, only the sum of \$3,400 being raised by the plaintiff, and the balance being raised by the defendant. The defendant took possession of the Madison avenue church, and held possession thereof until November 13, 1876, when possession was delivered to the plaintiff under the judgment in this case. It paid all of plaintiff's debts, except the sum of \$3,400 raised by plaintiff as above stated, the amount of its payments being upwards of \$68,000. During the whole time it maintained in its church all the services usual in Baptist churches. The church was at all times open to all, and most of plaintiff's former corporators and members attended and participated in the services there conducted.

In the summer of 1863 a majority of plaintiff's trustees having become dissatisfied with what had been done repudiated the conveyance, and the union of the churches, and commenced this action in plaintiff's name to recover back the property conveyed. The result has been that the plaintiff has recovered the possession of the property, and upon an accounting, conducted upon principles laid down by the court below, the defendant has been brought in debt to the plaintiff in the sum of \$9,681.20. The plaintiff has back all of its

property in good condition, free of debt, which, in 1875, was worth \$225,000; and the defendant, although acting in good faith, has lost all its property, owns no place of worship and is in debt to the plaintiff in the sum of nearly \$10,000. The result is somewhat extraordinary, and would seem to be quite inequitable. It was reached by holding the conveyance void, and then, upon the accounting, crediting defendant with the amount it paid upon the plaintiff's debts, and charging it with all pew rents received during about fourteen years, and allowing it nothing for the expenses of maintaining religious services in the church, which exceeded the amount of pew rents.

So far as I can perceive there was nothing illegal in the scheme, (but the conveyance of plaintiff's property.) Nothing else was done in violation of any law. The two ecclesiastical bodies could unite and be merged in one. New trustees could be elected, and they could go on and manage the church and maintain services therein. It was not illegal for plaintiff to put defendant in possession of its property upon some arrangement by which it was to maintain the services, and pay up plaintiff's debts, and it could even give the defendant a lien upon its property for any sums it might advance for plaintiff's benefit. (*Manning v. The Moscow Presbyterian Society*, 27 Barb. 52.) The plaintiff cannot recover back the property and also retain the consideration paid therefor. It was bound to restore to the defendant all it had received on account of the conveyance. This is not disputed. All the facts are set up in the answer, and equitable relief is demanded, and the account between the parties can be taken in this action. The defendant paid plaintiff's debts upon the faith of the title supposed to be conveyed, and upon the faith of the possession and enjoyment of the property, and in precise accordance with its agreement, and the court should not deprive it of this property until the plaintiff has in some way made restoration. There can be no moment of time when the plaintiff is entitled to have both the property and the consideration it received therefor. Restoration by the plaintiff should be a condition in such a case of restoration by the defendant. This, it seems to me, is demanded by general principles of equity and justice, and sanctioned by analogous cases. (*Gibert v. Peteler*, 38 N. Y. 165; *Mickles v. Dillaye*, 17 Id. 80; *Rose v. Watson*, 10 H. L. C. 672; *Dime v. Grace*, 5 DeG. & S. 451.) * * *

The judgment below must, therefore, be *affirmed*, so far as it judges the deed to the defendant invalid, and the title to be in the plaintiff; and in other respects it must be *reversed*, and the case must be remitted to the court below for an accounting upon the principles herein indicated, neither party to recover costs against the other in this court.

All concur, except ALLEN, J., not sitting, and MILLER, J., not voting.

Judgment accordingly.

MINERS' DITCH CO. v. ZELLERBACH.

1869. 37 Cal. 543.⁴

By the Court, SAWYER, C. J., on petition for rehearing: * * *

* * * The corporation having power to sell and convey its property, but it being made unlawful for the trustees to divide the capital stock, the corporation stood upon the same footing in respect to such conveyance as any natural person with reference to a contract, which he has the power to make, but which is made unlawful upon some principle of public policy adopted by the lawmaking power. In this case the contract was wholly executed. There was nothing of an executory character left on either side. The conveyance was fully made by the Miner's Ditch Company to the Eureka Lake Water Company, and the grantee put completely in possession, and remained for years in such possession with the knowledge and acquiescence of both the corporation and its stockholders. While so in possession, it executed its mortgage to Zellerbach and Powers, for the large sums of money advanced by them, and put them in possession, and this mortgage was subsequently foreclosed, and under the judgment of the court the property was sold and purchased in by them, and the defendant, having now acquired the entire title, is in possession. Large portions of the money advanced went in satisfaction of debts due from the Miners' Ditch Company. At all events, the defendant was in possession under his conveyance, and the contracts were all fully executed on both sides, each having received and enjoyed the consideration. There was nothing of an executory character left. It is not sought by either party in this action to recover on any branch of an executory contract—the usual form in which questions in such cases are presented. The question is which party, *in fact*, has the title as the case now stands, and, as between those parties, it is clearly in the defendant. We know of no instance in which the grantor has been able to recover at law when the contract has been fully executed, as in this case. A fortiori, he would not be entitled to relief in equity. But in the worst view that can be taken for the defendant the maxim applied in suits on illegal executory contracts, in *pari delicto potior est conditio possidentis*, or *defendentis*, would apply, and justify an affirmance of the judgment. But the defendant is in a better position than if sued, on an executory contract. (See *Schermerhorn v. Salmon*, 14 N. Y. 141.) The contract is fully executed on both sides, and the transaction closed between them. The case of *Inhabitants of Worcester v. Eaton*, 11 Mass. 368, is precisely in point. The only difference is, in that case the grantor in the illegal deed is a natural person, and here it is a corporation. But with reference to the inherent power of the two persons to make a conveyance of the property conveyed, the parties stand on the same footing. The vice in both convey-

⁴Only a portion of the opinion on the petition for rehearing is given.—Eds.

ances, if any there be, is that the contract is illegal for similar reasons. The principle is, therefore, the same. The consideration of the conveyance in the case cited was a composition of a felony. Yet the contract being fully executed, it was held to pass the title, and could not be avoided, so as to authorize a recovery by the grantor, or, which is the same thing, by the subsequent grantee of the grantor, and this, when an entry had been made for the very purpose of avoiding the deed. The case is in point, and we know of none to the contrary; besides, we believe it to be sound. * * *

Rehearing denied.

[NOTE.—This subject should be further considered in connection with some of the cases in the section following.—Eds.]

Section 3.—Ultra Vires Contracts.

EAST ANGLIAN R. CO. v. EASTERN COUNTIES R. CO.

1851. 11 Common Bench (2 J. Scott) 775.¹

JERVIS, C. J., now delivered the judgment of the court:—

This is an action of covenant. The declaration states, that, before the contract was made, there were four railway companies, each incorporated by a separate act of parliament,—The Lynn and Ely Railway Company, The Ely and Huntingdon Railway Company, The Lynn and Dereham Railway Company, and the defendants, The Eastern Counties Railway Company; that the Lynn and Ely Railway Company had introduced into parliament, upon their own petition, four bills for purposes connected with their railway; that the three first-named companies had agreed to amalgamate and form one company under the name and style of The East Anglian Railways Company; and that a bill was then pending in parliament, to give effect to such agreement. The declaration then states that the defendants, by an indenture under their common seal, between themselves and the plaintiffs (comprehending the three first-named companies, since amalgamated by act of parliament), covenanted with the plaintiffs (amongst other things) to take a lease of their railways, upon certain terms mentioned in the indenture, and to find the capital necessary for the construction of the extensions, branches, and works authorized to be constructed by the bills then pending in parliament, and to pay the costs of preparing and promoting such bills, whether the same should pass into law or not. The declaration further states that the bills were proceeded with; that two were passed; and that the costs of the bills, amounting to a large sum, had not been paid by the defendants to the plaintiffs.

The defendants set out the indenture upon oyer, and pleaded that

¹ Only the opinion is given.—Eds.

the plaintiffs had no authority to grant leases of their railways to the defendants; that they had been unable to obtain acts of parliament for that purpose; that they had abandoned all intention of so doing; and that several shareholders of the defendant's company (naming them) had not assented to the making or executing the indenture, or the agreement therein contained.

The plaintiffs demurred generally to this plea: and the question for the opinion of the court, is, whether, upon this record, the plaintiffs can maintain their action. We are of opinion that they cannot, and that the defendants are entitled to judgment.

The defendants are incorporated by the statute 6 & 7 W. 4, c. cvi., the first section of which enacts that certain persons shall be united into a company for making and maintaining the railway mentioned in that section, and other works by that act authorized, and for other purposes in that act declared, and for that purpose shall be one body corporate by the name and style of "The Eastern Counties Railway Company," and have perpetual succession, and a common seal.

The third section empowers the company to raise a sum of money for making and maintaining the said railway, and other works authorized by the act; and the 5th section directs the money so raised to be expended in and towards making and maintaining the said railway, and other works, and in otherwise carrying the act into execution. The money raised on mortgage is to be applied in the same way,—§ 246; and the profits of the company, after defraying the expenses of making, maintaining, and working the said railway, are to be accounted for and divided amongst the proprietors of the undertaking,—§§ 170, 171.

This act is a public act, accessible to all, and supposed to be known to all; and the plaintiffs must, therefore, be presumed to have dealt with the defendants with a full knowledge of their respective rights, whatever those rights may be.

It is clear that the defendants have a limited authority only, and are a corporation only for the purpose of making and maintaining the railway sanctioned by the act; and that their funds can only be applied for the purposes directed and provided for by the statute. Indeed, it is not contended that a company so constituted can engage in new trades not contemplated by their act: but it is said that they may embark in other undertakings, however various, provided the object of the directors be to increase the profits of their own railway.

This, in truth, is the same proposition, in another form; for, if the company cannot carry on a new trade, merely because it was not contemplated by the act, they cannot embark in other undertakings not sanctioned by their act, merely because they hope the speculation may ultimately increase the profit of the shareholders. They cannot engage in a new trade, because they are a corporation only for the purpose of making and maintaining The Eastern Counties Railway.

What additional power do they acquire from the fact that the undertaking may in some way benefit their line? Whatever be their object, or the prospect of success, they are still but a corporation for the purpose only of making and maintaining The Eastern Counties Railway: and if they cannot embark in new trades, because they have only a limited authority, for the same reason they can do nothing not authorized by their act, and not within the scope of their authority.

Every proprietor, when he takes shares, has a right to expect that the conditions upon which the act was obtained will be performed; and it is no sufficient answer to a shareholder, expecting his dividend, that the money has been expended upon an undertaking which at some remote period may be highly beneficial to the line. The public also has an interest in the proper administration of the powers conferred by the act. The comfort and safety of the line may be seriously impaired if the money supposed to be necessary, and destined by parliament for the maintenance of the railway, be expended in other undertakings not contemplated when the act was obtained, and not expressly sanctioned by the legislature.

If the contract is illegal, as being contrary to the act of parliament, it is unnecessary to consider the effect of dissentient shareholders; for, if the company is a corporation only for a limited purpose, and a contract like that under discussion is not within their authority, the assent of all the shareholders to such a contract, though it may make them all personally liable to perform such contract would not bind them in their corporate capacity, or render liable their corporate funds.

But it is said that it does not sufficiently appear upon this record that the bills in parliament, and for which the defendants covenanted to pay the costs, were not connected with the defendant's railway. If railway companies could embark in undertakings collateral to their main line, merely because the main line might in the result be benefited, there would be much in this objection; but, upon the view which we have above expressed, the objection cannot prevail.

We know that each of the four litigant companies has a separate act of parliament: we know that the statute incorporating the defendants' company gives no authority respecting the bills promoted by the plaintiffs: and we are, therefore, bound to say that any contract relating to such bills is not justified by the act of parliament, is not within the scope of the authority of the company as a corporation, and is therefore void.

For these reasons, we are of opinion that there ought to be judgment for the defendants.

*Judgment for the defendants.*³

³ MacGregor v. Official Manager of Deal etc. R. Co. (1852) 22 Law J. Rep. (N. S.) Q. B. 69, 16 Eng. Law & Eq. 180, *Accord.* Cf. Mayor etc. of Norwich v. Norfolk R. Co. (1855) 4 Ellis & Bl. 397, 30 Eng. Law & Eq. 120.—Eds.

ASHBURY RAILWAY CARRIAGE AND IRON CO. v. RICHE.

1875. L. R. 7 House of Lords 653.*

MR. JOHN ASHBURY had carried on at two places in Lancashire a very extensive business in making railway carriages and wagons, turn-tables, paints, crossings, and roofs, and other things of a like sort needed by a railway company, but had not been concerned in the construction of railways themselves.

A company called "The Ashbury Railway Carriage and Iron Company," incorporated under the Companies Act, 1862, was started for the purpose of buying Mr. John Ashbury's business.

A memorandum of association of the company, dated on the 12th of September, 1862, was drawn up. By the 3d clause of this memorandum of association the objects of the company were thus defined: "The objects for which the company is established are to make and sell, or lend on hire, railway-carriages and wagons, and all kinds of railway plant, fittings, machinery, and rolling-stock; to carry on the business of mechanical engineers and general contractors; to purchase and sell, as merchants, timber, coal, metals, or other materials; and to buy and sell any such materials on commission, or as agents."

In 1864 Mr. Riche, the defendant in error, was carrying on business in Belgium, in partnership with his brother (since deceased) as a railway contractor. On the 14th of March, 1864, the Belgium Government granted to certain persons named Gillon and Bertsoen a provisional concession for making a line of railway from Antwerp to Tournay, the payment of two sums of £4,000 and £16,000 being settled as what is called "caution money." The two concessionaries desired a company to be formed to carry this concession into effect. It was agreed that Messrs. Riche were to have the construction of the line; and in the early part of 1865 the two concessionaries and Messrs. Riche and the directors of the Ashbury Company met together, and agreed to form a company (*Societe Anonyme*) to work the concession. The arrangement was for the Ashbury Company to purchase the concession from Messrs. Gillon for £70,000, and to give the contract for its construction to Messrs. Riche, the company thus becoming, in fact, the contractor for the construction of the line. In this negotiation Mr. James Ashbury, one of the directors of the English company, represented that company, and entered into the contracts. Sir Cusack Roney afterwards acted in the same character.

The formation of a *societe anonyme* in Belgium, and the agreement with Messrs. Riche that they should construct the line—the Ashbury company undertaking to supply the *societe anonyme* with the requisite funds—was said to have been adopted because the rails, etc., supplied by a Belgian house would be free from the duty that

* Portions of opinion and concurring opinions omitted.—Eds.

the Belgium Government imposed on rails imported from England, and consequently the profit from the construction of the line would be increased. Messrs. Riche began and for some time continued the works for the construction of the line; and for some time, too, the Ashbury directors paid, in the name of their company, money to the societe anonyme to which Messrs. Riche had become entitled.

(Differences arose between the Ashbury Company's directors and the shareholders who claimed that the contract was unauthorized and denied any ratification thereof.)

The Company, however, dealing with the brothers Riche repudiated the contract for constructing the line as one *ultra vires*. Messrs. Riche brought an action for damages for breach of contract.

The Court of Exchequer, Baron Bramwell dissenting, found in favor of plaintiffs. The judgment was taken in error to the Exchequer Chamber and the justices being equally divided, the judgment stood *affirmed*. See L. R. 9 Ex. 224, 249. Error was then brought to this House.

THE LORD CHANCELLOR (Lord Cairns).—

My Lords, but for this difference of opinion among the learned Judges, I should have said that the only questions of law which arise in the case, the questions which appear to me to be sufficient altogether to dispose of the case, were of an extremely simple character. The action was brought by the Plaintiffs, who appear to be contractors in Belgium, and it was brought for damages for the breach of an agreement entered into between the Plaintiffs and the shareholders, constituting the Ashbury Railway Carriage and Iron Company, Limited.

These persons constituted a company established under the Joint Stock Companies Act of 1862. I think your Lordships will find it necessary to consider with some minuteness some of the leading provisions of that Act of Parliament. But, in the first place, you will find it convenient to ascertain the purposes for which this company was formed, and then the nature of the agreement, or contract, for the breach of which the present action was brought. * * *

Now, whatever may be the meaning of "carry on the business of mechanical engineers and general contractors," to my mind it clearly does not include the making of either of these contracts. It could only be held to do so by holding that the words "general contractors" authorized generally the making of any contracts; and this they certainly do not.

My Lords, I agree entirely, both with the description given here by Mr. Baron Bramwell of the nature of the contract and with the conclusion at which he arrived, that a contract of this kind was not within the words of the memorandum of association. In point of fact it was not a contract in which, as the memorandum of association implies, the limited company were to be the employed, they were the employers. They purchased the concession of a railway—an object not at all within the memorandum of association; and having

purchased that, they employed, or they contracted to pay, as persons employing, the Plaintiffs in the present action, as the persons who were to construct it. That was reversing entirely the whole hypothesis of the memorandum of association, and was the making of a contract not included within, but foreign to, the words of the memorandum of association.

Those being the results of the documents to which I have referred, I will ask your Lordships now to consider the effect of the Act of Parliament—the Joint Stock Companies Act of 1862—on this state of things. And here, my Lords, I cannot but regret that by the two Judges in the Court of Exchequer the accurate and precise bearing of that Act of Parliament upon the present case appears to me to have been entirely overlooked or misapprehended; and that in the Court of Exchequer Chamber, speaking of the opinion of those learned Judges who thought that the decision of the Court of Exchequer should be maintained, the weight which was given to the provisions of this Act of Parliament appears to me to have entirely fallen short of that which ought to have been given to it. Your Lordships are well aware that this is the Act which put upon its present permanent footing the regulation of joint stock companies, and more especially of those joint stock companies which were to be authorized to trade with a limit to their liability.

The provisions under which that system of limiting liability was inaugurated, were provisions not merely, perhaps I might say not mainly, for the benefit of the shareholders for the time being in the company, but were enactments intended also to provide for the interests of two other very important bodies; in the first place, those who might become shareholders in succession to the persons who were shareholders for the time being; and secondly, the outside public, and more particularly those who might be creditors of companies of this kind. And I will ask your Lordships to observe, as I refer to some of the clauses, the marked and entire difference there is between the two documents which form the title deeds of companies of this description—I mean the Memorandum of Association on the one hand, and the Articles of Association on the other hand. With regard to the memorandum of association, your Lordships will find, as has often already been pointed out, although it appears somewhat to have been overlooked in the present case, that that is, as it were, the charter, and defines the limitation of the powers of a company to be established under the act. With regard to the articles of association, those articles play a part subsidiary to the memorandum of association. They accept the memorandum of association as the charter of incorporation of the company, and so accepting it, the articles proceed to define the duties, the rights and the powers of the governing body as between themselves and the company at large, and the mode and form in which the business of the company is to be carried on, and the mode and form in which changes in the internal regulations of the company may from time to time be made. With re-

*Important
Language*

gard, therefore, to the memorandum of association, if you find anything which goes beyond that memorandum, or is not warranted by it, the question will arise whether that which is so done is ultra vires, not only of the directors of the company, but of the company itself. With regard to the articles of association, if you find anything which, still keeping within the memorandum of association, is a violation of the articles of association, or in excess of them, the question will arise whether that is anything more than an act extra vires the directors, but intra vires the company.

(The learned Lord proceeded to refer to various sections of the Joint Stock Companies Act of 1862, especially with reference to the memorandum of association.)

Of the internal regulations of the company the members of it are absolute masters, and, provided they pursue the course marked out in the Act, that is to say, holding a general meeting and obtaining the consent of the shareholders, they may alter those regulations from time to time; but all must be done in the way of alteration subject to the conditions contained in the memorandum of association. That is to override and overrule any provisions of the articles which may be at variance with it. The memorandum of association is, as it were, the area beyond which the action of the company cannot go; inside that area the shareholders may make such regulations for their own government as they think fit. * * *

Now, my Lords, bearing in mind the difference which I have just taken the liberty of pointing out to your Lordships between the memorandum and the articles, we arrive at once at all which appears to me to be necessary for the purpose of deciding this case. I have used the expressions extra vires and intra vires. I prefer either expression very much to one which occasionally has been used in the judgments in the present case, and has also been used in other cases, the expression "illegality."

In a case such as that which your Lordships have now to deal with, it is not a question whether the contract sued upon involves that which is malum prohibitum or malum in se, or is a contract contrary to public policy, and illegal in itself. I assume the contract in itself to be perfectly legal, to have nothing in it obnoxious to the doctrine involved in the expressions which I have used. The question is not as to the legality of the contract; the question is as to the competency and power of the company to make the contract. Now, I am clearly of opinion that this contract was entirely, as I have said, beyond the objects in the memorandum of association. If so, it was thereby placed beyond the powers of the company to make the contract. If so, my Lords, it is not a question whether the contract ever was ratified or was not ratified. If it was a contract void at its beginning, it was void because the company could not make the contract. If every shareholder of the company had been in the room, and every shareholder of the company had said, "That is a contract which we desire to make, which we authorize the directors to make, to which we sanc-

tion the placing the seal of the company," the case would not have stood in any different position from that in which it stands now. The shareholders would thereby, by unanimous consent, have been attempting to do the very thing which, by the Act of Parliament, they were prohibited from doing.

But, my Lords, if the shareholders of this company could not *ab ante* have authorized a contract of this kind to be made, how could they subsequently sanction the contract after it had, in point of fact, been made. I endeavored to follow as accurately as I could the very able argument of Mr. Benjamin at your Lordships' Bar on this point; but it appeared to me that this was a difficulty with which he was entirely unable to grapple. He endeavored to contend that when the shareholders had found that something had been done by the directors which ought not to have been done, they might be authorized to make the best they could of a difficulty into which they had thus been thrown, and therefrom might be deemed to possess power to sanction the contract being proceeded with. My Lords, I am unable to adopt that suggestion. It appears to me that it would be perfectly fatal to the whole scheme of legislation to which I have referred, if you were to hold that, in the first place, directors might do that which even the whole company could not do, and that then, the shareholders finding out what had been done, could sanction, subsequently, what they could not antecedently have authorized.

My Lords, if this be the proper view of the Act of Parliament, it reconciles, as it appears to me, the opinion of all the Judges of the Court of Exchequer Chamber; because I find Mr. Justice Blackburn, whose judgment was concurred in by two other Judges who took the same view, expressing himself thus: (1) "I do not entertain any doubt that if, on the true construction of a statute creating a corporation it appears to be the intention of the legislature, expressed or implied, that the corporation shall not enter into a particular contract, every Court, whether of law or equity, is bound to treat a contract entered into contrary to the enactment as illegal, and therefore wholly void, and to hold that a contract wholly void cannot be ratified." My Lords, that sums up and exhausts the whole case. In my opinion, beyond all doubt, on the true construction of the statute of 1862, creating this corporation, it appears that it was the intention of the Legislature, not implied, but actually expressed, that the corporation should not enter, having regard to its memorandum of association, into a contract of this description. If so, according to the words of Mr. Justice Blackburn, every Court, whether of law or equity, is bound to treat that contract, entered into contrary to the enactment, I will not say as illegal, but as *extra vires*, and wholly null and void, and to hold also that a contract wholly void cannot be ratified.

My Lords, that relieves me, and, if your Lordships agree with me, relieves your Lordships from any question with regard to ratification. I am bound to say that if ratification had to be considered I have

found in this case no evidence which to my mind is at all sufficient to prove ratification; but I desire to say that I do not wish to found my opinion on any question of ratification. This contract, in my judgment, could not have been ratified by the unanimous assent of the whole corporation.

* * * * *

Judgment reversed.

CORBETT v. SOUTH EASTERN, ETC., R. CO.'S
MANAGING COMMITTEE.

1906. L. R. (1906) 2 Ch. Div. 12.⁴

APPEAL from a decision of Farwell, J.

As the material sections of the various railway Acts, the contract in question, and the facts are fully set out in the report of the case in the Court below, the following summary will be sufficient to make the arguments and judgments intelligible:—

By s. 19 of the Bexley Heath Railway Act, 1887, the Bexley Heath Railway Company agreed with Sir H. Barron, his heirs and assigns (therein referred to as the owner), that the company would, unless otherwise agreed between the company and the owner, construct and maintain a station for both passengers and goods at a certain point of their railway; and in pursuance of this contract the company constructed a station known as the Well Hall Station.

In 1900 the company's railway and undertaking were by an Act of Parliament transferred to and became vested in the South Eastern Railway Company.

In October, 1900, the defendants entered into a written contract with the plaintiff whereby for valuable consideration they agreed to pull down the Well Hall Station and in lieu thereof to erect a new station nearer to property of the plaintiff which he was developing as a building estate. The defendants entered into this contract in good faith and in ignorance of the provisions of s. 19 of the Bexley Heath Railway Act, 1887; and as soon as the matter was brought to their knowledge they informed the plaintiff that they could not fulfil their contract with him on the ground that it was ultra vires. Thereupon the plaintiff commenced this action, claiming specific performance of the agreement of October, 1900, and alternatively damages for the breach thereof.

Sir H. Barron was dead, and it was admitted that his successors in title would not consent to the removal of Well Hall Station.

Farwell, J., held that the contract with Sir H. Barron did not create any public rights; that it was not illegal or ultra vires the

⁴Dissenting opinion of Romer, L. J., and concurring memorandum of Collins, M. R., omitted.—Eds.

defendants to contract with the plaintiff to remove the station at Well Hall without first obtaining the consent of Sir H. Barron, and that as such consent could not be obtained, the defendants were liable in damages to the plaintiff for the breach of their contract with him.

The defendants appealed.

COZENS-HARDY, L. J.—The short question in this appeal is whether an agreement dated October 13, 1900, by which the defendant company purported to agree with the plaintiff (*inter alia*) to discontinue the use of the present Well Hall Station and in lieu thereof to erect a new station, is *ultra vires* and, therefore, illegal by reason of s. 19 of the Bexley Heath Railway Act, 1887. The defendant company is the successor of the Bexley Heath Railway Company and subject to all the obligations of that company. Sect. 19, so far as material, is in the following words: "For the protection of Sir Henry Page Turner Barron, Baronet, his heirs and assigns (hereinafter referred to as and included in the expression 'the owner'), the following provisions shall unless otherwise agreed between the company and the owner have effect (that is to say)." Then sub-s. 4 is: "The company shall construct and maintain a station for both passengers and goods, with all proper and sufficient works and accommodation and access to and from the estate of the owner, at the point of junction of the railway authorized by this Act with railway No. 1 authorized by the Act of 1883, or as near thereto as the levels and other circumstances will permit." It is urged on the part of the appellants that s. 19 contains a statutory obligation which is still in force to maintain the station which, by the contract of October, 1900, the appellants have agreed to remove, and that it makes no difference that the obligation imposed by s. 19 might be waived or released by Sir Henry Barron. In other words, the appellants urge that there is a statutory conditional prohibition against doing that which they purport to bind themselves to do by the contract in question, and that, unless and until the condition is got rid of, the contract is *ultra vires* and illegal. On the other hand it is urged that, when s. 19 is looked at, it is nothing more than a private bargain between the company and Sir Henry Barron; that it contains no term which was not within the competence of the railway company, and that no rights are conferred thereby upon the public, and that it ought to be regarded as having no greater or other effect than a contract under seal between the company and Sir Henry Barron in the precise terms of s. 19 and not mentioned in the Act of Parliament would have had. Farwell, J., has adopted the latter view, and held the company liable to pay damages, although the plaintiff cannot obtain specific performance.

Now it is important to observe that the Bexley Heath Railway Company, though incorporated in 1883, had no power to take the land or made the railway mentioned in s. 19 except under the powers and subject to the restrictions contained in the Bexley Heath

Railway Act, 1887, and the acts incorporated therewith. A railway company is an artificial person incorporated by statute, and the limits of its powers are prescribed either expressly or by implication by statute. In the language of Lord Watson in *Baroness Wenlock v. River Dee Co.*, "Whenever a corporation is created by Act of Parliament, with reference to the purposes of the Act, and solely with a view to carrying these purposes into execution, I am of opinion not only that the objects which the corporation may legitimately pursue must be ascertained from the Act itself, but that the powers which the corporation may lawfully use in furtherance of these objects must either be expressly conferred or derived by reasonable implication from its provisions." A contract not within the limits as above defined is *ultra vires*, illegal, and wholly void: *Riche v. Ashbury Railway Carriage and Iron Co., Ltd.* It is not necessary to find words of prohibition to render such a contract illegal, but the presence of such words is important as establishing beyond doubt that such a contract is not within the powers of the company. It is well known that railway Acts frequently confirm a schedule contract, and it may be that in such a case the contract, though confirmed by statute, will, for some purposes, have no further or greater effect than a contract not confirmed by statute: See per Lord Watson in *Davis & Sons, Ltd. v. Taff Vale Ry. Co.* The observations of Lord Watson were, however, addressed to the point whether any third person had a right conferred upon him by such a statutory contract; and they have no direct bearing upon the question of *ultra vires*. But where the statute does not confirm a schedule contract, but contains an express enactment imposing certain obligations upon the company, it is not, in my opinion, necessary for the purpose of the doctrine of *ultra vires* to consider whether they are imposed for the benefit of the public or a class of the public or for a private individual owning a particular estate. The effect of the statutory obligations upon the powers of the company must in each case be the same. Nor does it make any difference that by the terms of the statute the obligations may be varied or released by agreement between the company and a private individual. The obligations remain, until varied, statutory obligations. *Joseph Crosfield & Sons, Ltd. v. Manchester Ship Canal Co.* is an illustration of this. Farwell, J., has held that s. 19 constitutes merely a contract between the company and Sir Henry Barron, and that no question of *ultra vires* arises. With great respect for the learned judge, I am unable to assent to this view. Sect. 19 is not in form an agreement. It is in form a statutory enactment, and none the less so because its terms may be varied by agreement between the company and Sir Henry Barron. The section has not been varied, and it therefore remains in full force. The company's powers to take and use the lands and to make the railway were subject to the conditions found in s. 19. It is not competent to the company to take the land and then to do that which the statute has

prohibited, and, in my opinion, it makes no difference that the prohibition was not in the interest of the general public, but for the protection of a private owner. If the company had only agreed with the plaintiff to use their best endeavors to procure a release by Sir Henry Barron from the obligations imposed by s. 19, and, in the event of such release being procured, then to discontinue the use of the present Well Hall Station, such an agreement might not have been ultra vires. But I cannot hold that this is the effect of the agreement of October, 1900, nor can I regard the objection as simply one of title. The question of defect of title can only arise if there is a valid contract; and it has no relevance where the doctrine of ultra vires negatives the existence of a contract.

For these reasons I think the appeal must be allowed and the action dismissed with costs here and below.

NASSAU BANK v. JONES.

1884. 95 N. Y. 115.*

APPEAL from judgment of the General Term of the Superior Court of the City of New York, entered upon an order made April 9, 1883, which affirmed a judgment in favor of defendants, entered upon a decision of the court on trial at Special Term. (Reported below, 17 J. & S. 498.)

This action was brought against defendants as executors of the will of Daniel Jones to compel them to transfer and deliver to plaintiff fifty \$1,000 bonds and one hundred and twenty-five shares of the stock of the Denver and Rio Grande Railroad Company, or to account for and pay over the value thereof and all interests and dividends received by their testator thereon.

The material facts are stated in the opinion.

RUGER, Ch. J.—The question involved in this case, as we regard it, is the right of a banking corporation chartered under the laws of this state to subscribe for the stock of a railroad corporation.

In the spring of 1879, the Denver and Rio Grande Railroad Company, being a corporation organized to construct railroads in Colorado and adjoining territories, with the view of raising money to extend its lines, published a circular, whereby it proposed in substance, to issue \$5,000,000, of its bonds, in sums of \$1,000 each, payable thirty years after date, with annual interest at seven per cent. in gold, secured by mortgage upon its property; and to deliver one of such bonds together with five shares of its capital stock, of the par value of \$100, per share, to each and every person who should advance thereon the sum of \$900, reserving, however, the privilege to the railroad company, of withdrawing the proposition, when it should

* Portion of opinion omitted.—Eds.

have received subscriptions to said loan, to the amount of \$3,000,000. This proposal was favorably received, and the loan was subscribed for by citizens and corporations in various States of the union, to an amount greatly exceeding the sum required by the railroad company. Among others the defendants' testator, one David Jones, subscribed for, and was awarded \$90,000, of such contemplated loan. It is claimed by the appellant, and was found as a fact by the trial court, that Jones undertook, by the authority and for the benefit of the plaintiff, to contract with this railroad company, for a loan, under its proposal, in the name of the plaintiff, to the extent of one-half of the amount which should be allotted to him; and by this action the appellant seeks to recover, from Jones' executors, among other things, the profits claimed to have been made by him upon its share of the transaction. The right to maintain the action seems to depend upon the power of the bank to enter into the proposed contract, for if it had no lawful authority to make such a contract it could not become liable to Jones upon its obligation to take and pay for the property contracted for; and consequently there would be no consideration for Jones' undertaking to subscribe for the benefit of the bank. Not only this, but the bank could not, by suit, enforce against any one an executory contract which it was unauthorized by its charter to make.

It becomes necessary, therefore, to inquire into the nature of the proposed contract, and the legal capacity of the plaintiff to transact business.

The proposition of the railroad company contemplated either a loan of money, or a sale of its stocks and bonds; and the view we take of the case does not render it material to determine which construction should be given. By whatever name it be called, the transaction contemplated that its subscribers should become the legal owners of the certain stock and bonds thereby offered to be disposed of.

If it be regarded as a loan, the subscriber would receive the bonds with their mortgage security, as an evidence of the company's indebtedness to him; and the stock as a bonus to induce the making of the loan. On the other hand, if it be considered as a purchase of the stock and securities of the railroad corporation, the subscriber becomes the owner of such stock and bonds upon complying with the conditions of the proposition.

In either event he becomes the absolute owner of the property proposed to be delivered in exchange for the money advanced, and acquires all the rights and privileges, and subjects himself to all the liabilities of such proprietorship.

The acquisition by the railroad of a new class of stockholders, was as much a part of the scheme as the creation of a debt; and its proposition to loan money could not be availed of, under the terms of the offer without necessarily involving an acceptance of the privileges, and incurring the liabilities of a stockholder. The offer of this stock was a material part of the proposition, and was undoubtedly largely relied upon as an inducement to investors. The increase of creditors

and stockholders would proceed *pari passu*, under this scheme; and the subscribers to the loan might, in case of the company's insolvency, eventually, as the owners of its stock, be compelled to contribute to the payment of its debts.

It is clear that a banking corporation cannot enter into a contract of this character, unless it has authority under its charter to become a subscriber for the stock of railroad corporations, and thereby assume the obligations to which stockholders are subject by statute. (*Adderly v. Storm*, 6 Hill 624.)

It is scarcely conceivable that it can be seriously urged, that a moneyed corporation, having under its charter the right to transact a banking business only, may legally engage, as a corporation, in the construction of railroads, or in furnishing money for such an object, in exchange for the stock of a railroad corporation, and yet when this case is analyzed and stripped of its irrelevant details and circumstances, we cannot see why this is not precisely what was attempted by the plaintiff.

This action is brought upon the theory that Jones was, in making the subscription in question, the agent of the plaintiff, and it thereby seeks to charge the defendants, as Jones' executors, with a trusteeship for its benefit, of a large quantity of the stock of the railroad corporation, for which it asks the defendants to account to it, as the owners thereof.

The complaint assumes, that the plaintiff, in 1879, became the equitable owner of a large amount of such stock, acquired by virtue of an original subscription therefor made with the company issuing the stock; and that it has ever since been the equitable owner, and is now entitled to demand the immediate delivery and possession of such stock.

Assuming the validity of the contract relied upon by the plaintiff, it has been for several years a stockholder in the railroad company, and has thereby become answerable as such stockholder, for a moiety at least, of any sum which Jones might be required to pay, through any statutory liability for the debts of the corporation. (*Stover v. Flack*, 30 N. Y. 64.)

Even a cursory view of the provisions of the statute under which the plaintiff was organized, and the cases giving construction to the powers thereby conferred, renders it quite clear, that the contract under which the plaintiff claims was not only *ultra vires*, but contrary to public policy.

(The learned judge held that "the utmost liberality in the construction of the powers" conferred upon moneyed corporations would not include the rights claimed.)

For these reasons, we are of the opinion that the plaintiff was not only precluded by public policy, but was not authorized by the statute under which it was organized, to enter into any engagement as a stockholder in a railroad corporation.

The contract between the plaintiff and Jones was wholly executory,

and nothing has occurred thereunder, preventing the bank from setting up its own want of authority to make such a contract, as a defense to any action brought thereon by Jones.

While executed contracts, made by corporations in excess of their legal powers, have, in some cases, been upheld by the courts, and parties have been precluded from setting up, as a defense to actions brought by corporations, their want of power to enter into such contracts (*Bissell v. M. S. & N. I. R. R. Co.*, 22 N. Y. 258; *Whitney Arms Co. v. Barlow*, 63 id. 62; *Woodruff v. E. R. Co.*, 93 id. 618), this doctrine has never been applied to a mere executory contract which is sought to be made the foundation of an action, either by or against such corporations. It was said by Judge Selden, in *Tracy v. Talmage* (14 N. Y. 179), "That a contract by a corporation, which it has no legal capacity to make, is void and cannot be enforced, it would seem difficult to deny." In *White v. Buss* (3 Cushing 448), Chief Justice Shaw lays down the rule as follows: "It is well settled by the authorities that any promise, contract or undertaking, the performance of which would tend to promote, advance or carry into effect an object or purpose which is unlawful, is in itself void and will not maintain an action."

Lord Mansfield, in *Smith v. Bromley* (Douglas 696), says: "If the act is in itself immoral, or a violation of the general laws of public policy, then the party paying shall not have this action." In *Tracy v. Talmage* (supra 217), Judge Comstock says: "It is admitted that the contract of a corporation, which it has no legal capacity to make, cannot in its terms be enforced."

There is nothing in this case to exempt the plaintiff from the operation of the general principle determined in the cases referred to.

Jones owed no duty to the plaintiff, except that which sprang out of his engagement to purchase the stock and bonds in question; and that having failed on account of its illegality, left no enforceable obligation resting upon him. (*Levy v. Brush*, 45 N. Y. 589.) There is no pretext for the claim that the contract was in any respect an executed one, for Jones never even entered upon its performance. His subscription for the loan in his own name was in direct violation of the obligation which it is claimed that he had assumed; and it is that obligation alone which is sought to be enforced in this action. The bank, by the transaction in question, secured Jones' promise to do certain things, and has relied solely upon that promise. It has done nothing in performance of the contract, and, so far as it is concerned, the contract remains wholly executory.

Neither can Jones be treated as a trustee for the benefit of the plaintiff, a trust whereby it is attempted to accomplish an illegal purpose, is quite as objectionable as a direct contract to effect the same object.

The law does not raise an implied obligation to effectuate a purpose which is forbidden, and which cannot be effected by the parties through the agency of an express contract. (*Perry on Trusts*, § 214.)

The claim here is that a trust should be implied to enable the plaintiff to reap the profits from a transaction in which it was not authorized by law to engage. We have found no authority which supports such a claim and are unable to discover any ground upon which this action can be maintained.

It follows that the judgment should be affirmed.

All concur, except RAPALLO and EARL, JJ., dissenting.

Judgment affirmed.

BOWMAN DAIRY CO. v. MOONEY.

1890. 41 Mo. App. 665.

BIGGS, J.—The Bowman Dairy Company is a Missouri corporation, and it is authorized to carry on a dairy business in the city of St. Louis. The present action is one in equity, and was instituted by the Bowman Dairy Company, as plaintiff, to restrain the defendant from violating a certain contract alleged to have been entered into by the plaintiff and the defendant. There was a temporary injunction, which was dissolved upon a final hearing, when the plaintiff's action was dismissed. From this judgment the plaintiff has prosecuted an appeal.

In the petition the defendant was charged with the violation of the following written contract: "This agreement made this twelfth day of September, 1889, between the Bowman Dairy Company, of the first part, and, of the second part, both of the city of St. Louis and state of Missouri, witnesseth: That the said Bowman Dairy Company does hereby employ the said J. T. Mooney as driver of an oyster wagon, and agrees to pay him eighteen dollars per week. Said J. T. Mooney, in consideration of the above sum of eighteen dollars per week, during his employment by said Bowman Dairy Company, hereby agrees to drive such oyster wagon, and perform such duties as may be assigned to him by said Bowman Dairy Company, its officers or agents; to use all diligence in his power to make and keep trade for the Bowman Dairy Company; and at no time whilst in their employ, or within two years after leaving their service, to sell oysters for himself or any other person or company to the customers of first part, or interfere with or enter into competition with their business, or in any way, directly or indirectly, divert, take away, or attempt to divert or take away, any of their custom or patronage. This contract as to the terms of service may be terminated by either party giving thirty days' notice.

"(Signed) JOHN T. MOONEY,
"BOWMAN DAIRY CO.

"By J. R. BOWMAN,
"Secretary."

The execution of the contract was admitted. The plaintiff's evidence tended to prove that the defendant entered upon the discharge

of his duties under this contract of employment, and that he worked two days, earned six dollars, collected two dollars from the company, and then quit work without any cause or excuse. The evidence also tended to show that the defendant soon thereafter commenced to sell oysters on his own account to plaintiff's customers. To prevent the continuation of this the present proceeding was begun.

In defense of the action, and on a hearing of a motion to dissolve the temporary injunction, the defendant introduced the plaintiff's articles of association, which showed that the plaintiff was incorporated under article 8, chapter 42, of the Revised Statutes of 1889, entitled "Manufacturing and business companies;" that the name adopted by the plaintiff was the "Bowman Dairy Company;" that the purposes of the corporation were: First. "To buy and sell dairy products, especially milk, butter, cheese and ice cream." Second. "To purchase, hold, mortgage or otherwise convey such real estate and personal property, as the purposes of the corporation shall require."

The plaintiff introduced additional evidence, which had a tendency to show the following state of facts: That on the twelfth day of September, 1889, the plaintiff purchased the stock in trade of the firm of Berry & Owens, which firm had been engaged for some years in the wholesale and retail oyster business in the city of St. Louis; that said firm had built up a large and lucrative trade; that the plaintiff, in making such purchase, also bought the good will of the firm; that for several years the defendant had been in the employ of Berry & Owens, as the driver of one of their oyster wagons in a certain district in the city; that, by reason of such employment, the defendant had become well acquainted with the customers of the firm along his routes; that, before making the purchase from Berry & Owens, the plaintiff made the foregoing contract with the defendant; that they would not have made said purchase, had it not been for the contract with defendant, and that this was known to the defendant at the time he entered into the agreement.

The doctrine of ultra vires was invoked by the defendant as a defense to the action. The defendant denied the plaintiff's right to the aid of a court of equity in the enforcement of the contract against him for the reason, that the plaintiff's charter confined its business to the sale of milk, butter, cheese, etc.; that it was, therefore, prohibited by law from engaging in the oyster business; and that, as the contract pertained to the latter business, it was ultra vires of the corporation, and, as the contract was yet in fieri, its enforcement would violate a rule of public policy. On the other hand the plaintiff insisted that the law, under which it was incorporated, did not confine its business to dealings in dairy products, but that it was authorized to engage in any business "intended for pecuniary profit or gain, not otherwise especially provided for, and not inconsistent with the constitution and laws of this state." R. S. 1889, § 2771. The argument is, therefore, made that the proviso found in the general statute in relation to corporations (Revised Statutes, 1889, § 2508), to the effect

that no corporation shall engage in business other than that expressly authorized by its charter, or the law under which it was organized, can in no way invalidate the plaintiff's action in the purchase of the oyster business, for the reason that such business is lawful, that it is not otherwise especially provided for, and that, as it is a business of pecuniary gain or profit, its exercise was within the powers conferred upon the plaintiff by the statute under which it was incorporated. It is further insisted that, if it be conceded that the purchase of the oyster business by the plaintiff was outside its corporate powers, yet the judgment of the court is wrong, because the evidence showed that the contract had been fully performed by the plaintiff, that the defendant had received and accepted its gains and advantages, and that consequently a court of equity should decree its enforcement. The plaintiff urges two additional arguments against the finding of the circuit court: First. That the defendant ought not to be heard in such a defense, for the reason that the plaintiff, on account of his contract, was induced to change its position, whereby great loss will be caused to the plaintiff, if the defendant is allowed to prevail in this action; in other words, that the defendant ought to be estopped by his contract. Second. That, if the plaintiff has violated its charter, the state alone can take advantage of it in a direct proceeding to declare a forfeiture. The foregoing is the statement, as we understand them, of the theories of the respective parties concerning the law applicable to this case.

I. It is a well-established principle that all corporate acts, not expressly granted to a corporation by legislative enactments, are prohibited by the common law; therefore, when a corporation derives its authority either from a special act of the legislature, or by virtue of a general law, to prosecute a particular business, in a particular way, it is as much incapacitated from engaging in another business as if it had not been incorporated at all. Any business prosecuted by a corporation must be expressly authorized by its charter, or must in some way be necessary to the successful prosecution of the business mentioned. *Ashbury, etc., Railway Co. v. Riche*, 44 L. J. Exch. 185; *Oregon Railway and Navigation Co. v. Railroad*, 130 U. S. 1. This is elementary law. The plaintiff's articles of association expressly authorize it to engage in buying and selling dairy products, especially milk, butter, cheese and ice cream, and to purchase and hold such real and personal property as the purposes of its business may require. It must be conceded that the oyster business cannot by any possible construction be held to be in aid of, or necessary to, the successful prosecution of the dairy business. * * * Our conclusion is that the plaintiff had no right to engage in the oyster business, and that the contract with the defendant in reference thereto was ultra vires of the corporation.

II. The next proposition is that, although the contract was void for want of power on the plaintiff's part to execute it, nevertheless, since it has been fully executed by the plaintiff, a court of equity will

decree its enforcement. This rule is stated by Mr. Morawetz in his work on corporations, section 689, as follows: "After a contract entered into by a corporation has been performed by either of the contracting parties, the fact that the making of the contract involved an unauthorized exercise of corporate power on the part of the company will not constitute a defense to an action brought by the party having performed the contract to recover compensation for a breach by the other party." The principle involved in this rule has been the subject of much judicial discussion, which has resulted in some confusion in the authorities. We think that a great deal of this confusion has arisen from a misconception of the true principle upon which the rule is predicated. So long as such a contract is executory, that is, when it has not been fully performed by either party, the courts will not sustain any kind of action based upon it. The reason is that the enforcement of such a contract would be against public policy, and in direct violation of law. As was said by Judge Miller in *Case v. Kelly*, 133 U. S. 28: "While a court might hesitate to declare the title to lands already received, and in the possession and ownership of the company, void on the principle that they had no authority to take such lands, it is very clear that it will not make itself the active agent in behalf of the company in violating the law and enabling the company to do that which the law forbids." See, also, *Thomas v. Railroad*, 101 U. S. 71, 86. Some authorities proceed on the idea that the rule is in some way founded on the law governing estoppels. Reasoning from this premise, it has been stated in a general way that the defense of ultra vires should not prevail, when its enforcement would be inequitable, thereby losing sight of the true principle upon which the whole doctrine rests. It is from this standpoint that the plaintiff's counsel make the argument, that the contract must be considered as fully performed by the plaintiff, or that the defendant should be estopped to set up the defense of ultra vires. Mr. Morawetz (2. Mor. Corp. 692) says: "The rule is not based upon the doctrine of estoppel, as has sometimes been suggested. An estoppel in pais involves a representation of a fact upon the faith of which an innocent party has been induced to alter his position. The rule referred to, however, applies where both parties to the contract have notice that it was in excess of the charter powers of the corporation, and, therefore, prohibited by law. * * * Moreover, the doctrine of estoppel cannot be invoked by an individual so as to defeat the operation of a rule of law established for the benefit of the community in general. The legal prohibition against the unauthorized exercise of corporate powers is established for the benefit of the public, on general grounds of expediency, and not for the benefit of corporations, or of persons dealing with them. The effect of the prohibition upon a contract, therefore, depends wholly upon the requirements of the public policy pursuant to which the prohibition was established." If we apply the principle announced, the contract in the case at bar will not be enforced in any way against the defendant merely because it would

work an injustice to the plaintiff to allow the defendant to recede from it. In order to defeat the defendant it must appear that plaintiff has fully performed the contract. If such be the case, then the infraction of the law has already taken place, which would eliminate all questions of public policy from the case, and allow the courts to deal with the contract on equitable principles. Under this view the question at the threshold is, did the defendant have the right to recede from the contract at the time he quit work? Or, to put it in another way, was the contract at that time fully performed by the plaintiff? If the answer to this proposition is against the plaintiff, the facts and circumstances, under which the contract was entered into, and the effect of its violation by the defendant, become immaterial inquiries.

Did the defendant have the right to recede from the contract? When an individual is sued upon a contract by a corporation, he is permitted to make the defense of ultra vires upon the theory that, at the time of its violation by him, there was no legal obligation on the part of the corporation to comply with its part of the contract. In other words there is a want of mutuality in the contract. *Whitney Arms Co. v. Barlow*, 63 N. Y. 62. When such a contract has been fully performed by the corporation, the mutuality of the obligation becomes an immaterial question for the reason, that the defendant can have no occasion to seek its enforcement. It is upon this idea, together with other reasons heretofore mentioned by us, that courts make a distinction between executory and executed contracts, when dealing with the question of ultra vires. Applying what we have said to the contract in issue, it becomes quite apparent that the defendant was at liberty to repudiate it at the time he quit work. At that time the contract was in fieri, and the plaintiff had the undoubted right to discharge the defendant from its employment, and in such an event he would have been without a remedy. This conclusively shows that there was no mutuality of obligation existing, and it is decisive of the point in favor of the defendant. This result cannot be avoided by the argument that the consideration for the latter portion of the defendant's undertaking had passed to him. It would not comport with our ideas of the law to say to the defendant that, although he had no rights under the contract, nevertheless a court of equity would compel him to quit selling oysters on his own account by reason of the contract. * * *

What we have said disposes of the objection that the defendant cannot avail himself of the plea of ultra vires. When the action is based on a contract, which is shown to be beyond the powers of the corporation, and which remains executory, we have found no case, which goes to the extent of holding that the individual cannot allege the illegality of the contract in opposition to its enforcement.

*Judgment affirmed.**

* See also *Screven Hose Co. v. Philpot* (1875) 53 Ga. 625; *Case v. Kelly* (1890) 133 U. S. 21.—Eds.

CENTRAL TRANSPORTATION CO. v. PULLMAN'S
PALACE CAR CO.1890. 139 U. S. 24, 35 L. ed. 55, 11 Sup. Ct. 478.⁷

ACTION of covenant by the Central Transportation Co., a corporation of Pennsylvania, against Pullman's Palace Car Co., a corporation of Illinois, to recover the sum of \$198,000, due for the last three-quarters of the year ending July 1, 1886, according to the terms of an indenture of lease from the plaintiff of all its personal property to the defendant, dated February 17, 1870.

The plaintiff was originally organized under the general laws of Pennsylvania which provided for the incorporation of companies "for the purpose of carrying on the manufacture of woolen, cotton, flax or silk goods, or of iron, paper, lumber or salt", or "for the manufacture of articles from iron and other metals, or out of wood, iron and other metals."

The plaintiff's certificate of incorporation stated the object for which it was formed to be "the transportation of passengers in railroad cars constructed and to be owned by the said company in accordance with the several letters patent," which it owned.

By special act of the legislature subsequently passed, the charter of the company was extended and it was "empowered to enter into contracts with corporations of this or any other state for the leasing or hiring and transfer to them, or any of them of their railway cars and other personal property."

The defendant was incorporated under a special act of the legislature of Illinois "to manufacture, construct and purchase railway cars, with all convenient appendages and supplies for persons traveling therein and the same to sell or use or permit to be used, in such manner and upon such terms as the said company may think fit and proper."

On February 17, 1870, an indenture of lease was entered into between the two companies whereby the plaintiff leased all its sleeping cars with their equipment, its contracts, its patent rights and all its other "personal property, rights, credits, moneys and effects," etc., to the defendant for the term of ninety-nine years, covenanting further not to "engage in the business of manufacturing, using or hiring sleeping cars," during the said term.

The defendant, on its part, covenanted inter alia to pay to plaintiff annually the sum of \$264,000.

At the trial, plaintiff offered evidence tending to show that the defendant had entered into possession of plaintiff's property under the lease, and had continued in possession during the period set forth in the declaration. Defendant's objection to this evidence, "on the ground that it was beyond the power of either corporation to make the contract," was sustained, and plaintiff excepted. De-

⁷ Statement abridged. Portions of opinion omitted.—Eds.

defendant's motion for a non-suit was granted and from the judgment entered thereon plaintiff appeals.

MR. JUSTICE GRAY, after stating the case as above, delivered the opinion of the court.

The principal defence in this case, duly made by the defendant, by formal plea, as well as by objection to the plaintiff's evidence, and sustained by the Circuit Court, was that the indenture of lease sued on was void in law, because beyond the powers of each of the corporations by and between whom it was made. * * *

It was therefore rightly assumed by the counsel of both parties at the argument that the only question to be determined is of the correctness of the ruling sustaining the defense of ultra vires, independently of the form in which that question was presented and disposed of.

Upon the authority and the duty of a corporation to exercise the powers granted to it by the legislature, and those only; and upon the invalidity of any contract, made beyond those powers, or providing for their disuse or alienation; there is no occasion to refer to decisions of other courts, because the judgments of this court, especially those delivered in the last twelve years by the late Mr. Justice Miller, afford satisfactory guides and ample illustrations.

(The learned judge proceeded to consider these decisions in detail.)

The clear result of these decisions may be summed up thus: The charter of a corporation, read in the light of any general laws which are applicable, is the measure of its powers, and the enumeration of those powers implies the exclusion of all others not fairly incidental. All contracts made by a corporation beyond the scope of those powers are unlawful and void, and no action can be maintained upon them in the courts, and this upon three distinct grounds: the obligation of every one contracting with a corporation, to take notice of the legal limits of its powers; the interest of the stockholders, not to be subjected to risks which they have never undertaken; and, above all, the interest of the public, that the corporation shall not transcend the powers conferred upon it by law. A corporation cannot, without the assent of the legislature, transfer its franchise to another corporation, and abnegate the performance of the duties to the public, imposed upon it by its charter as the consideration for the grant of its franchise. (Neither the grant of a franchise to transport passengers, nor a general authority to sell and dispose of property, empowers the grantee, while it continues to exist as a corporation, to sell or to lease its entire property and franchise to another corporation.) These principles apply equally to companies incorporated by special charter from the legislature, and to those formed by articles of association under general laws.

* * * The plaintiff, therefore, was not an ordinary manufacturing corporation, such as might, like a partnership or an indi-

vidual engaged in manufactures, sell or lease all its property to another corporation. *Ardesco Oil Co. v. North American Oil Co.*, 66 Penn. St. 375; *Treadwell v. Salisbury Manuf. Co.*, 7 Gray 393. But the purpose of its incorporation, as defined in its charter, and recognized and confirmed by the legislature, being the transportation of passengers, the plaintiff exercised a public employment, and was charged with the duty of accommodating the public in the line of that employment, exactly corresponding to the duty which a railroad corporation or a steamboat company, as a carrier of passengers, owes to the public, independently of possessing any right of eminent domain. The public nature of that duty was not affected by the fact that it was to be performed by means of cars constructed and of patent rights owned by the corporation, and over roads owned by others. The plaintiff was not a strictly private, but a quasi public corporation; and it must be so treated as regards the validity of any attempt on its part to absolve itself from the performance of those duties to the public, the performance of which by the corporation itself was the remuneration that it was required by law to make to the public in return for the grant of its franchise. *Pickard v. Pullman Southern Car Co.*, 117 U. S. 34; *York & Maryland Railroad v. Winans*, 17 How. 30, 39; *Railroad Co. v. Lockwood*, 17 Wall. 357; *Liverpool & Great Western Steam Co. v. Phenix Ins. Co.*, 129 U. S. 397.

The evident purpose of the legislature, in passing the statute of 1870, was to enable the plaintiff the better to perform its duties to the public, by prolonging its existence, doubling its capital, and confirming, if not enlarging, its powers. An intention that it should immediately abdicate those powers, and cease to perform those duties, is so inconsistent with that purpose, that it cannot be implied, without much clearer expressions of the legislative will looking towards that end, than are to be found in this statute.

The provision of this statute, by which the plaintiff is empowered to contract with other corporations "for the leasing or hiring and transfer to them, or any of them," of its "railway cars and other personal property," is fully satisfied by construing it as confirming the plaintiff's right to do as it had been doing, to "lease" or "hire" (which are equivalent words) to other corporations in the regular course of its business, and to "transfer" under such leasing or hiring, its "railway cars," and "other personal property," either connected with the cars, or at least of the same general nature of tangible property. It can hardly be stretched to warrant the plaintiff in making to a single corporation an absolute transfer, or a long lease, of all that might be comprehended in the words "personal property" in their widest sense, including not only goods and chattels, but moneys, credits and rights of action. In any view, it would be inconsistent alike with the main purpose of the statute, and with the uniform course of decision in this court, to construe these words as authorizing the plaintiff to deprive itself, either absolutely, or for a long period of time, of the

right to exercise the franchise granted to it by the legislature for the accommodation of the public. * * *

Considering the long term of the indenture, the perishable nature of the property transferred, the large sums to be paid quarterly by the defendant by way of compensation, its assumption of the plaintiff's debts, and the frank avowal, in the indenture itself, of the intention of the two corporations to prevent competition and to create a monopoly, there can be no doubt that the chief consideration for the sums to be paid by the defendant was the plaintiff's covenant not to engage in the business of manufacturing, using or hiring sleeping cars; and that the real purpose of the transaction was, under the guise of a lease of personal property, to transfer to the defendant nearly the whole corporate franchise of the plaintiff, and to continue the plaintiff's existence for the single purpose of receiving compensation for not performing its duties.

The necessary conclusion from these premises is, that the contract sued on was unlawful and void, because it was beyond the powers conferred upon the plaintiff by the legislature, and because it involved an abandonment by the plaintiff of its duty to the public. * * *

The contract sued on being clearly beyond the powers of the plaintiff corporation, it is unnecessary to determine whether it is also ultra vires of the defendant, because, in order to bind either party, it must be within the corporate powers of both. *Thomas v. Railroad Co.*, *Pennsylvania Railroad v. St. Louis &c. Railroad*, and *Oregon Railway v. Oregonian Railway*, above cited.

It was argued in behalf of the plaintiff that, even if the contract sued on was void, because ultra vires and against public policy, yet that, having been fully performed on the part of the plaintiff, and the benefits of it received by the defendant, for the period covered by the declaration, the defendant was estopped to set up the invalidity of the contract as a defense to this action to recover the compensation agreed on for that period.

But this argument, though sustained by decisions in some of the states, finds no support in the judgments of this court.

(The learned judge then reviewed the Federal decisions.)

In *Pittsburgh &c. Railway v. Keokuk & Hamilton Bridge*, it was stated, as the result of the previous cases in this court, that "a contract made by a corporation, which is unlawful and void because beyond the scope of its corporate powers, does not, by being carried into execution, become lawful and valid, but the proper remedy of the party aggrieved is by disaffirming the contract and suing to recover, as on a quantum meruit, the value of what the defendant has actually received the benefit of." 131 U. S. 371, 389.

The view which this court has taken of the question presented by this branch of the case, and the only view which appears to us consistent with legal principles, is as follows:

A contract of a corporation, which is ultra vires, in the proper sense, that is to say, outside the object of its creation as defined in the

law of its organization, and therefore beyond the powers conferred upon it by the legislature, is not voidable only, but wholly void, and of no legal effect. The objection to the contract is, not merely that the corporation ought not to have made it, but that it could not make it. The contract cannot be ratified by either party, because it could not have been authorized by either. No performance on either side can give the unlawful contract any validity, or be the foundation of any right of action upon it.

When a corporation is acting within the general scope of the powers conferred upon it by the legislature, the corporation, as well as persons contracting with it, may be estopped to deny that it has complied with the legal formalities which are prerequisites to its existence or to its action, because such requisites might in fact have been complied with. But when the contract is beyond the powers conferred upon it by existing laws, neither the corporation, nor the other party to the contract, can be estopped, by assenting to it, to show that it was prohibited by those laws.

The doctrine of the common law, by which a tenant of real estate is estopped to deny his landlord's title, has never been considered by this court as applicable to leases by railroad corporations of their roads and franchises. It certainly has no bearing upon the question whether this defendant may set up that the lease sued on, which is not of real estate, but of personal property, and which includes, as inseparable from the other property transferred, the inalienable franchise of the plaintiff, is unlawful and void, for want of legal capacity in the plaintiff to make it.

A contract ultra vires being unlawful and void, not because it is in itself immoral, but because the corporation, by the law of its creation, is incapable of making it, the courts, while refusing to maintain any action upon the unlawful contract, have always striven to do justice between the parties, so far as could be done consistently with adherence to law, by permitting property or money parted with on the faith of the unlawful contract, to be recovered back, or compensation to be made for it. See 331.

In such case, however, the action is not maintained upon the unlawful contract, nor according to its terms; but on an implied contract of the defendant to return, or, failing to do that, to make compensation for, property or money which it has no right to retain. To maintain such an action is not to affirm, but to disaffirm, the unlawful contract.

The ground and the limits of the rule concerning the remedy, in the case of a contract ultra vires, which has been partly performed, and under which property has passed, can hardly be summed up better than they were by Mr. Justice Miller in a passage already quoted, where he said that the rule "stands upon the broad ground that the contract itself is void, and that nothing which has been done under it, nor the action of the court, can infuse any vitality into it;" and that "where the parties have so far acted under such a contract that they

cannot be restored to their original condition, the court inquires if relief can be given independently of the contract, or whether it will refuse to interfere as the matter stands." *Pennsylvania Railroad v. St. Louis &c. Railroad*, 118 U. S. 317.

Whether this plaintiff could maintain any action against this defendant, in the nature of a quantum meruit, or otherwise, independently of the contract, need not be considered, because it is not presented by this record, and has not been argued. This action, according to the declaration and the evidence, was brought and prosecuted for the single purpose of recovering sums which the defendant had agreed to pay by the unlawful contract, and which, for the reasons and upon the authorities above stated, the defendant is not liable for.

Judgment affirmed.^a

NATIONAL HOME BLDG. & LOAN ASSN. v. HOME SAVINGS BANK.

1899. 181 Ill. 35, 54 N. E. 619.*

MR. CHIEF JUSTICE CARTWRIGHT delivered the opinion of the court:

In November, 1893, Flora D. Bishopp made a trade of lots in the city of Chicago with the National Home Building and Loan Association, appellant, in pursuance of which appellant conveyed to her lot 10 in Lee Bros.' addition to Englewood, lots 15 and 16 in block 60 in Chicago University subdivision, and lot 36 in block 2, Herring's subdivision. In exchange for these lots said Flora D. Bishopp and Jonathan D. Bishopp, her husband, conveyed to the building and loan association lots 5 and 6 in block 2 in Johnson & Clement's subdivision, and in the deed of the same it was agreed that the building and loan association should assume and pay an encumbrance on said lot 5 in the form of a trust deed executed by said Flora D. Bishopp and husband to Charles T. Page, trustee, to secure a note for \$3,000 and interest. The trade was negotiated and carried out on the part of the association through J. O. Duncan, agent, who was employed by the association to negotiate loans and examine abstracts for it in Chicago, and he acted under the direction of the secretary of

*In accord with the rule of the Federal courts, *Chewacla Lime Works v. Dismukes* (1888) 87 Ala. 344, 6 So. 122; *New York etc. Ins. Co. v. Ely* (1825) 5 Conn. 560; *Best Brewing Co. v. Klassen* (1900) 185 Ill. 37, 57 N. E. 20 (*cf.* *Peoria Star Co. v. Cutright* (1904) 115 Ill. App. 492); *In re Assignment of Mutual etc. Ins. Co.* (1899) 107 Ia. 143, 77 N. W. 868 (corporation not liable on *ultra vires* insurance policy although premium paid); *Greenville etc. Warehouse Co. v. Planters' etc. Warehouse Co.* (1893) 70 Miss. 669, 13 So. 879; *Norton v. Derry Nat. Bank* (1882) 61 N. H. 589; *Marble Co. v. Harvey* (1892) 92 Tenn. 115, 20 S. W. 427; *Metropolitan Stock Exchange v. Lyndonville Nat. Bank* (1903) 76 Vt. 303, 57 Atl. 101. See also *Slater Woollen Co. v. Lamb* (1887) 143 Mass. 420, 9 N. E. 823.—Eds.

^aPortions of opinion omitted.—Eds.

the association. After the exchange the association paid a mortgage of \$600 on said lot 5 and the delinquent interest on the mortgage assumed in the conveyance. On May 14, 1895, the board of directors passed a resolution that the assumption clause in the deed was made without authority of the association, and directed the execution and tender of a quit-claim deed of the lot to Flora D. Bishopp. The deed was made and tendered unconditionally, and the association thereby offered the lot to her without a return of the consideration or any other condition. The note for \$3,000, secured by the trust deed, was transferred to the Home Savings Bank, one of the appellees, and it filed its bill in the superior court of Cook county to foreclose the same, asking for a decree against Flora D. Bishopp, a sale of the mortgaged premises, and a decree against the building and loan association for such deficiency as might exist. The building and loan association answered that the trade was consummated by direction of its president and secretary, but the clause assuming the mortgage was inserted without their knowledge or authority and without the knowledge and authority of its board of directors, that such an agreement was *ultra vires* the corporation, and that it had tendered a quit-claim deed of the lot to the said Flora D. Bishopp. The bill was answered by Flora D. Bishopp and her husband, who admitted its material allegations and filed their cross-bill, alleging the agreement for an exchange of the properties and the conveyances and asking for a deficiency decree against the association. The building and loan association answered the cross-bill, setting up the same defense as before, and the cause was referred to a master, who reported in favor of a foreclosure and sale and a decree against the building and loan association for any deficiency in the payment of the debt, interest, fees and costs. Exceptions to the report were overruled and a decree was entered in accordance with it, which has been affirmed by the Appellate Court.

No objection is made to the foreclosure of the trust deed or the sale of the premises, and the only question involved in this appeal is whether the contract inserted in the deed, by which the defendant, the National Home Building and Loan Association, agreed to assume and pay the debt, is binding upon it. This defendant, which denied the binding force of the agreement, is a corporation organized under the provisions of an act entitled "An act to enable associations of persons to become a body corporate to raise funds to be loaned only among the members of such association," in force July 1, 1879. (Laws of 1879, p. 83.) As a corporation it is a creature of the law, having no powers but those which the law has conferred upon it. A corporation has no natural rights or capacities, such as an individual or an ordinary partnership, and if a power is claimed for it, the words giving the power or from which it is necessarily implied must be found in the charter or it does not exist. The law on this subject is stated by the Supreme Court of the United States in *Central Transportation Co. v. Pullman Palace Car Co.*, 139 U. S. 24, as follows: "The char-

ter of a corporation, read in the light of any general laws which are applicable, is the measure of its powers, and the enumeration of those powers implies the exclusion of all others not fairly incidental." The purpose of this corporation is the raising of funds to be loaned to its members upon the security of its stock and unencumbered real estate. Manifestly the business of trading in real estate or acquiring the same, except as incidental to their legitimate business, is wholly foreign to the purpose for which the State has created such corporations and conferred upon them corporate powers. They have no power to take and hold real estate, and contracts made for the purchase of it are not enforceable. (Endlich on Building Associations, secs. 305-308.) But for the purpose of collecting debts it is essential that they should have some power with respect to the real estate mortgaged to them, and for that purpose section 13 of the act for their incorporation provides as follows: "Any loan or building association incorporated by or under this act is hereby authorized and empowered to purchase at any sheriff's or other judicial sale, or any other sale, public or private, any real estate upon which such association may have or hold any mortgage, lien or other encumbrance, or in which said association may have an interest, and the real estate so purchased, to sell, convey, lease or mortgage at pleasure to any person or persons whatsoever." Such corporations are not authorized, either by their charters or as an incident to their existence, to acquire or hold any real estate, except such as has been mortgaged to them or which they may have an interest in. Not only is this the rule to be derived from the act of the legislature authorizing their incorporation, under the general principles of law, but it is, and always has been, against the policy of the state to permit corporations to accumulate landed estates, or to own real estate beyond what is necessary for their corporate business or such as is acquired in the collection of debts. (*Carroll v. City of East St. Louis*, 67 Ill. 568; *United States Trust Co. v. Lee*, 73 id. 142; *People v. Pullman Palace Car Co.*, 175 id. 125; *First M. E. Church of Chicago v. Dixon*, 178 id. 260.) It is also a settled principle of American jurisprudence. (5 *Thompson's Law of Corporations*, sec. 5772.) If a building and loan association were permitted to invest its money in the purchase of real estate or to traffic or trade in such property instead of keeping within the powers conferred upon it by loaning such money and collecting it, it would not only be exercising powers not granted, but it would be carrying on a business inconsistent with the purpose of its creation and against the fixed and uniform policy of the state. In *People ex rel. v. Chicago Gas Trust Co.*, 130 Ill. 268, it was said (p. 292): "The word 'unlawful', as applied to corporations, is not used exclusively in the sense of *malum in se* or *malum prohibitum*. It is also used to designate powers which corporations are not authorized to exercise, or contracts which they are not authorized to make, or acts which they are not authorized to do—or, in other words, such acts, powers and contracts as are *ultra vires*."

It is also argued that the building and loan association is estopped to raise the question whether the contract was *ultra vires* because it has received the benefit of the contract by the conveyance of property to it. That depends, as we think, upon the sense in which the term *ultra vires* is used. It has been applied indiscriminately to different states of fact in such a way as to cause considerable confusion. When used as applicable to some conditions, it has been frequently said that a corporation is estopped to make such a defense where it has received the benefit of the contract. For example, the term has been applied to acts of directors or officers which are outside and beyond the scope of their authority, and therefore are invasions of the rights of stockholders, but which are within the powers of the corporation. In such a case the act may become binding by ratification, consent and acquiescence, or by the corporation receiving the benefit of the contract. Again, it has been applied to cases where an act was within the authority of the corporation for some purposes or under some circumstances, and where one dealing in good faith with the corporation had a right to assume the existence of the conditions which would authorize the act. Where an act is not *ultra vires* for want of power in the corporation but for want of power in the agent or officer, or because of the disregard of formalities which the law requires to be observed, or in an improper use of one of the enumerated powers, it may be valid as to third persons. In the more proper and legitimate use of the term it applies only to acts which are beyond the purpose of the corporation, which could not be sanctioned by the stockholders. There would, of course, be no power to confirm or ratify a contract of that kind, because the power to enter into it is absolutely wanting. If there is no power to make the contract there can be no power to ratify it, and it would seem clear that the opposite party could not take away the incapacity and give the contract vitality by doing something under it. It would be contradictory to say, that a contract is void for an absolute want of power to make it and yet it may become legal and valid as a contract, by way of estoppel, through some other act of the party under such incapacity, or some act of the other party chargeable by law with notice of the want of power.

The powers delegated by the State to the corporation are matters of public law, of which no one can plead ignorance. A party dealing with a corporation having limited and delegated powers conferred by law is chargeable with notice of them and their limitations, and cannot plead ignorance in avoidance of the defense. (*Franklin Co. v. Lewiston Institution for Savings*, 68 Me. 43; *New Orleans, Florida and Havana Steamship Co. v. Ocean Dry Dock Co.*, 28 La. Ann. 173.) Concerning this subject it is said in *Thomas v. West Jersey Railroad Co.*, 101 U. S. 71: "To hold that this can be done is, in our opinion, to hold that any act done under a void contract makes all its parts valid, and that the more you do under a contract forbidden by law the stronger the claim to its enforcement in the courts." * * * In *Durkee v. People*, 155 Ill. 354, the same rules were laid down, and it

was pointed out that the cases where a corporation is estopped from asserting that a contract is ultra vires when it has received a benefit under the contract is where the making of the contract is within the scope of the franchise, and the contract is sought to be avoided because there was a failure to comply with some regulation or the power was improperly exercised. The following was there quoted from the opinion in *Davis v. Old Colony Railroad Co.*, 131 Mass. 258: "There is a clear distinction, as was pointed out by Mr. Justice Campbell in *Zabriskie v. Cleveland, Columbus and Cincinnati Railroad Co.*, by Mr. Justice Hoar in *Monument Bank v. Globe Works*, and by Lord Chancellor Cairns and Lord Hatherley in *Ashbury Railway Carriage and Iron Co. v. Riche*, between the exercise by a corporation of a power not conferred upon it, varying from the objects of its creation as declared in the law of its organization, of which all persons dealing with it are bound to take notice, and the abuse of a general power or the failure to comply with prescribed formalities or regulations in a peculiar instance, when such abuse or failure is not known to the other contracting parties."

The cases in this court where the corporation has been held to be estopped have been where the act complained of was within the general scope of the corporate powers.

(The learned judge considered the Illinois decisions.)

In this case the transaction was beyond the corporate powers and ultra vires in the strict and legitimate sense, and against public policy. It could not be ratified or become valid by acquiescence, since there was no power to make it. *Flora D. Bishopp*, who dealt with the corporation, was chargeable with notice of its powers and their limitations and its inability to enter into the contract. She could not make the void contract valid by acting under it. No action can be maintained upon the unlawful contract, and in such cases, if the courts can afford any remedy, it cannot be done by affirming or enforcing the contract, but in some other manner.

The decree of the superior court against the National Home Building and Loan Association for any deficiency that may exist, and for execution to collect the same, and the judgment of the Appellate Court affirming said decree in that respect, are each reversed.

Judgment reversed.

MR. JUSTICE CARTER, dissenting:

I do not agree to the doctrine announced in the decision of this case, that a corporation may not be estopped from pleading its own lack of corporate power. As I understand the decisions, it has long been the settled doctrine of this court that where the contract has been wholly executed and the corporation has received the benefit of it, it will be estopped from setting up in defense of payment its own lack of power, under its charter, to enter into the contract, where the contract is not one either *malum in se* or *malum prohibitum*. I do not understand that the application of the doctrine of estoppel is confined to those cases where the contract is within the powers of the corpo-

ration, but only beyond the mere authority of its officers or agents. The doctrine of estoppel does not rest upon the principle of agency that there may be a ratification of the unauthorized acts of agents. It has been held, not only by this court but by many others, that in many cases the question of ultra vires can only be raised in a direct proceeding by the State to oust the corporation of its assumed and usurped powers. *Bradley v. Ballard*, 55 Ill. 413; *Kadish v. Garden City Building Assn.*, 151 id. 531; *McNulta v. Corn Belt Bank*, 164 id. 427; *Eckman v. Chicago, Burlington and Quincy Railroad Co.*, 169 id. 312; *Darst v. Gale*, 83 id. 136.

NATIONAL BANK v. MATTHEWS.

1878. 98 U. S. 621, 25 L. ed. 188.

ERROR to the Supreme Court of the State of Missouri.

On the 1st of March, 1871, Hugh B. Logan and Elizabeth A. Matthews executed and delivered to Sterling Price & Co. their joint and several promissory note for the sum of \$15,000, payable to the order of that firm two years from date, with interest at the rate of ten per cent. per annum. The payment of the note was secured by a deed of trust, executed by her, of certain real estate therein described, situate in the State of Missouri.

On the 13th of the same month, the note and deed of trust were assigned to the Union National Bank of St. Louis. Price & Co. failed to pay the loan at maturity. The bank directed the trustee named in the deed of trust to sell. Said Elizabeth thereupon filed this bill in the proper state court to enjoin the sale. The bank in its answer avers that it "accepted the said note and deed of trust as security for the sum of \$15,000, then and there advanced and loaned to said Sterling Price & Co. * * * on the security of said note and deed of trust." A perpetual injunction was decreed, upon the ground that the loan by the bank to Price & Co. was made upon real-estate security; that it was forbidden by law; and that the deed of trust was, therefore, void. The decree was made upon the pleadings. No testimony was introduced upon either side. The bank removed the case to the Supreme Court of the State, where the decree was affirmed. The bank then sued out this writ of error.

MR. JUSTICE SWAYNE, after stating the facts, delivered the opinion of the court.

This case involves a question arising under the national banking law, which has not heretofore been passed upon by this court. We have considered it with the care due to its importance.

Our attention has been called to but a single point which requires consideration, and that is, whether the deed of trust can be enforced for the benefit of the bank.

The statutory provisions which bear upon the subject are as follows:—

"SECT. 5136." Every national banking association is authorized "to exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this title.

"SECT. 5137. A national banking association may purchase, hold, and convey real estate for the following purposes, and for no others: First, such as may be necessary for its immediate accommodation in the transaction of its business. Second, such as shall be mortgaged to it in good faith by way of security for debts previously contracted. Third, such as shall be conveyed to it in satisfaction of debts previously contracted in the course of its dealings. Fourth, such as it shall purchase at sales under judgments, decrees, or mortgages held by the association, or shall purchase to secure debts to it. But no such association shall hold the possession of any real estate under mortgage, or the title and possession of any real estate purchased to secure any debts due to it for a longer period than five years." Rev. Stat. 1909; 13 Stat. 99.

Here the bank never had any title, legal or equitable, to the real estate in question. It may acquire a title by purchasing at a sale under the deed of trust; but that has not yet occurred, and never may.

Sect. 5137 has, therefore, no direct application to the case. It is only material as throwing light upon the point to be considered in the preceding section. Except for that purpose it may be laid out of view.

Sect. 5136 does not, in terms, prohibit a loan on real estate, but the implication to that effect is clear. What is so implied is as effectual as if it were expressed. As the transaction is disclosed in the record, the loan was made upon the note as well as the deed of trust. *Non constat*, that the maker who executed the deed would not have been deemed abundantly sufficient without the further security. The deed, as a mortgage would have been, was an incident to the note, and a right to the benefit of the deed, whether mentioned or delivered or not, when the note was assigned, would have passed with the note to the transferee of the latter.

The object of the restrictions was obviously threefold. ¹ It was to keep the capital of the banks flowing in the daily channels of commerce; ² to deter them from embarking in hazardous real-estate speculations; and to prevent the accumulation of large masses of such property in their hands, to be held, as it were, in mortmain. The intent, not the letter, of the statute constitutes the law. A court of equity is always reluctant in the last degree to make a decree which will effect a forfeiture. The bank parted with its money in good faith. Its garments are unspotted. Under these circumstances, the defense

of *ultra vires*, if it can be made, does not address itself favorably to the mind of the Chancellor. We find nothing in the record touching the deed of trust which, in our judgment, brings it within the letter or the meaning of the prohibitions relied upon by the counsel for the defendant in error.

In *The First National Bank of Fort Dodge v. Haire and Others* (36 Iowa, 443), the bank refused to discount a note for a firm, but agreed that one of the partners might execute a note to the other, that the payee should indorse it, that the bank should discount it, and that the maker should indemnify the indorser by a bond and mortgage upon sufficient real estate executed for that purpose, with a stipulation that, in default of due payment of the note, the bond and mortgage should inure to the benefit of the bank. The arrangement was carried out. The note was not paid. The maker and indorser failed and became bankrupts. The bank filed a bill to foreclose. The same defence was set up as here. In disposing of this point, the Supreme Court of the State said: "Every loan or discount by a bank is made in good faith, in reliance, by way of security, upon the real or personal property of the obligors; and unless the title by mortgage or conveyance is taken to the bank directly, for its use, the case is not within the prohibition of the statute. The fact that the title or security may inure indirectly to the security and benefit of the bank will not vitiate the transaction. Some of the cases upon quite analogous statutes go much further than this. *Silver Lake Bank v. North*, 4 J. C. R. 370."

But it is alleged by the learned counsel for the defendant in error that in the jurisprudence of Missouri a deed of trust is the same thing in effect as a direct mortgage,—with respect to a party entitled to the benefit of the security,—and authorities are cited in support of the proposition. The opinion of the Supreme Court of Missouri assumes that the loan was made upon real-estate security within the meaning of the statute, and their judgment is founded upon that view. These things render it proper to consider the case in that aspect. But, conceding them to be as claimed, the consequence insisted upon by no means necessarily follows. The statute does not declare such a security void. It is silent upon the subject. If Congress so meant, it would have been easy to say so; and it is hardly to be believed that this would not have been done, instead of leaving the question to be settled by the uncertain result of litigation and judicial decision. Where usurious interest is contracted for, a forfeiture is prescribed and explicitly defined.

In *Harris v. Runnels* (12 How. 79), this court said that "the statute must be examined as a whole, to find out whether or not the makers meant that a contract in contravention of it was to be void, so as not to be enforced in a court of justice." In that case, a note given for the purchase money of slaves, taken into Mississippi contrary to a statute of the State, was held to be valid.

Where a statute imposes a penalty on an officer for solemnizing a

marriage under certain circumstances, but does not declare the marriage void, the marriage is valid; but the penalty attaches to the officer who did the prohibited act. *Milford v. Worcester*, 7 Mass. 48; *Parton v. Hervey*, 1 Gray (Mass.), 119; *King v. Birmingham*, 8 Barn. & Cress. 29.

Where a bank is limited by its charter to a specified rate of interest, but no penal consequence is denounced for taking more, it has been held that a contract for more is not wholly void. *The Planters' Bank v. Sharp et al.*, 12 Miss. 75; *The Grand Gulf Bank v. Archer et al.*, 16 Id. 151; *Rock River Bank v. Sherwood*, 10 Wis. 230.

The charter of a savings institution required that its funds should be "invested in, or loaned on, public stocks or private mortgages," etc. A loan was made and a note taken, secured by a pledge of worthless bank-stock. The borrower sought to enjoin the collection of the note upon the ground that the transaction was forbidden by the charter, and therefore void. The court held the borrower bound, and upon a counter-claim adjudged that he should pay the amount of the loan with interest. *Mott v. The United States Trust Co.*, 19 Barb. (N. Y.) 568.

Where a corporation is incompetent by its charter to take a title to real estate, a conveyance to it is not void, but only voidable, and the sovereign alone can object. It is valid until assailed in a direct proceeding instituted for that purpose. *Leazure v. Hillegas*, 7 Serg. & R. (Pa.) 313; *Goundie v. Northampton Water Co.*, 7 Pa. St. 233; *Runyon v. Coster*, 14 Pet. 122; *The Banks v. Poitiaux*, 3 Rand. (Va.) 136; *McIndoe v. The City of St. Louis*, 10 Mo. 577. See also *Gold Mining Company v. National Bank*, 96 U. S. 640.

The authority first cited is elaborate and exhaustive upon the subject. So an alien, forbidden by the local law to acquire real estate, may take and hold title until office found. *Fairfax's Devisee v. Hunter's Lessee*, 7 Cranch, 604.

In *Silver Lake Bank v. North* (4 Johns. (N. Y.) Ch. 370), the bank was a Pennsylvania corporation, and had taken a mortgage upon real estate in New York. A bill of foreclosure was filed in the latter State. The answer set up as a defence "that by the act of incorporation the plaintiffs were not authorized to take a mortgage except to secure a debt previously contracted in the course of its dealings; and here the money was lent after the bond and mortgage were executed." The analogy of this defence to the one we are considering is too obvious to need remark. Both present exactly the same question. Chancellor Kent said: "Perhaps it would be sufficient for this case that the plaintiffs are a duly incorporated body, with authority to contract and take mortgages and judgments; and if they should pass the exact line of their power, it would rather belong to the government of Pennsylvania to exact a forfeiture of their charter, than for this court in this collateral way to decide a question of misuser, by setting aside a just and *bona fide* contract."

* * * "If the loan and mortgage were concurrent acts, and in-

tended so to be, it was not a case within the reason and spirit of the restraining clause of the statute, which only meant to prohibit the banking company from vesting their capital in real property, and engaging in land speculations. A mortgage taken to secure a loan advanced *bona fide* as a loan, in the course and according to the usage of banking operations, is not surely within the prohibition."

It is not denied that the loan here in question was within this category. This authority, if recognized as sound, is conclusive. See also *Baird v. The Bank of Washington*, 11 Serg. & R. (Pa.) 411.

Sedgwick (Stat. and Const. Constr. 73) says: "Where it is a simple question of authority to contract, arising either on a question of regularity of organization or of power conferred by the charter, a party who has had the benefit of the agreement cannot be permitted in an action founded upon it to question its validity. It would be in the highest degree inequitable and unjust to permit a defendant to repudiate a contract, the benefit of which he retains."

What is said in the text is fully sustained by the authorities cited.

We cannot believe it was meant that stockholders, and perhaps depositors and other creditors, should be punished and the borrower rewarded, by giving success to this defence whenever the offensive fact shall occur. The impending danger of a judgment of ouster and dissolution was, we think, the check, and none other contemplated by Congress.

That has been always the punishment prescribed for the wanton violation of a charter, and it may be made to follow whenever the proper public authority shall see fit to invoke its application. A private person cannot, directly or indirectly, usurp this function of the government.

The decree of the Supreme Court of Missouri will be reversed, and the cause remanded with directions to dismiss the bill; and it is *So ordered*.¹⁰

MR. JUSTICE MILLER dissenting.

I am of opinion that the National Banking Act makes void every mortgage or other conveyance of land as a security for money loaned by the bank at the time of the transaction to whomsoever the

¹⁰ *Beach v. Wakefield* (1899) 107 Ia. 567, 76 N. W. 688, 78 N. W. 197; *Washington Life Ins. Co. v. Clason* (1900) 162 N. Y. 305, 56 N. E. 755, *Accord*.

WILKS v. GEORGIA PACIFIC R. Co. (1885) 79 Ala. 180. Bill by the railway company for the specific performance of a contract by which defendants agreed to convey in consideration of the railway company's completing its road to a named point within a specified time. The road was completed, as agreed, and within the time specified. *Held*, the bill must be dismissed. Stone, C. J., said (p. 187): "The case, then, presents the naked question, whether a corporation, without express power therefor, can sue on an executory contract, and recover an interest in lands, when it does not appear that such land or interest is necessary for carrying into effect some power or purpose for which the corporation was created. Our uniform rulings for forty years require us to answer the question in the negative."—Eds.

conveyance may be made; that the bank is forbidden to accept such security, and it is void in its hands.

The contract to pay the money, and the collateral conveyance for security, are separable contracts, and so far independent that one may stand and the other fall.

In the present case, the money was loaned on the faith of the deed of trust, and that instrument is void in the hands of the bank, but the note, as evidence of the loan of money, is valid against Mrs. Matthews personally. With this latter contract the state court did not interfere. It enjoined proceedings under the deed of trust against the land, and did no more.

Its judgment in that matter ought, in my opinion, to be affirmed.

WHITNEY ARMS CO. v. BARLOW.

1875. 63 N. Y. 62.¹¹

The American Seal and Lock Co., a corporation organized under the general manufacturing act of New York (chap. 40, Laws of 1848), entered into a contract with plaintiff, the Whitney Arms Co., a corporation organized in the State of Connecticut "for the purpose of manufacturing every variety of fire-arms and other implements of war, caps, cartridges, balls and like munitions of war applicable to the use of fire-arms, and all kinds of machinery adapted for the construction thereof and otherwise," by which the latter company agreed to manufacture and deliver 20,000 railroad locks to be paid for sixty days after delivery. Plaintiff made and delivered 10,000 locks under the contract when, by mutual agreement, the contract was suspended as to the residue. The American Seal & Lock Co. gave two notes for the purchase price, and having failed to pay its notes, this action was brought against the defendants as trustees to enforce their statutory liability for this indebtedness of the corporation.

ALLEN, J.—* * * It must be conceded that the manufacturing and vending of "railroad locks" is not within the purposes for which the plaintiff was incorporated, or within the powers conferred by its charter. Neither is such business incidental to the purposes of the incorporation, or in any way necessary to, or as far as appears even an aid in the exercise of the powers conferred upon the plaintiff by its constitution, so that it could be regarded as among the implied powers granted by the legislature and assumed by the corporators.

Did the question now made arise upon an application by the stockholders and corporators to restrain the corporate agents from applying the corporate funds to purposes foreign to the corporation, or en-

¹¹ Statement rewritten. Portions of opinion omitted.—Eds.

gaging in business outside of that for which the company was formed, or on proceedings by the sovereign power to annul the charter for an abuse of the powers granted, or in a proceeding to enforce and for the performance of an executory contract, where, upon a rescission or annulling the agreement, both parties would have the same position as if no contract had been made, the rules of decision would be different from those which must prevail in the present action. In either of the cases suggested it is very likely the courts would be compelled to give full effect to the objection and hold the business unauthorized and a violation of the charter, and a forfeiture of the chartered rights and the contract null, and refuse to perform it or give effect to it. The manufacture of the locks, or contract to sell them to the Seal Lock Company, were not acts immoral in themselves or forbidden by any statute, neither *mala in sese* or *mala prohibita*, so as to make the contract illegal and incapable of being the foundation of an action; such a contract as the law will not recognize or enforce, but applying the maxim, *ex facto illicito non oritur actio*, leave the parties as it finds them.

When acts of corporations are spoken of as ultra vires, it is not intended that they are unlawful or even such as the corporation cannot perform, but merely those which are not within the powers conferred upon the corporation by the act of its creation, and are in violation of the trust reposed in the managing board by the shareholders, that the affairs shall be managed and the funds applied solely for carrying out the objects for which the corporation was created. (*Earl of Shrewsbury v. North Staffordshire R. Co.*, L. R. 12, 1 Eq., 593; *Taylor v. Chichester and Midhurst R. Co.*, L. R., 2 Exch., 356; *Bissell v. Mich. C. R. Co.*, 22 N. Y. 258.)

Whether the contract as originally made was ultra vires is not a very important inquiry at this time. If it was, the State under whose sovereignty it dwells and by whose act and favor it exists, has no interest in arresting its action for the recovery of moneys equitably due upon a contract fully executed and a work fully accomplished, whatever may be its right to annul its charter. The shareholders, whose confidence has been abused and whose funds have been diverted from their proper use, have a direct interest in reclaiming and restoring to proper custody and applying to legitimate uses the funds which have been diverted and improperly used for purposes de hors the legitimate business of the corporation. The plea of ultra vires should not as a general rule prevail, whether interposed for or against a corporation, when it would not advance justice, but on the contrary would accomplish a legal wrong.

Here, as between two corporations, the debtor and creditor corporation, the contract has been fully performed by the creditor, the plaintiff in this action, and the Seal Lock Company has received the full consideration of its promise to pay. The plaintiff has parted with its property to the latter corporation, and unless a legal liability exists on the part of the latter to pay, the plaintiff can neither re-

claim the property or recover compensation, and under this technical plea a great wrong will be perpetrated. A purchaser who acquired by contract, and under an agreement to pay for it, the property of a corporation, cannot defeat the claim for the purchase-price by impeaching the right of the corporation to become the owner of the property. (One who has received from a corporation the full consideration of his engagement to pay money, either in services or property, cannot avail himself of the objection that the contract thus fully performed by the corporation was ultra vires, or not within its chartered privileges and powers.) It would be contrary to the first principles of equity to allow such a defence to prevail in an action by the corporation.

It is now very well settled that a corporation cannot avail itself of the defence of ultra vires when the contract has been, in good faith, fully performed by the other party, and the corporation has had the full benefit of the performance and of the contract. If an action cannot be brought directly upon the agreement, either equity will grant relief or an action in some other form will prevail. The same rule holds *e converso*. If the other party has had the benefit of a contract fully performed by the corporation, he will not be heard to object that the contract and performance were not within the legitimate powers of the corporation. (Ex parte Chippendale, 4 D. G., M. & G., 19; In re National P. B. Build. Soc., L. R., 5 Chy. Appeals, 309; In re Cork, etc., R. C., 4 id., 748; Fishmongers Co. v. Robertson, 5 McG., 131.)

The only justification for such a plea by an individual sued upon a contract with a corporation is, that the obligation is not mutual, as the other party, the corporation, would not be bound by it. The objection to such a defence in an action upon an executed contract is given by Tindal, Ch. J., in the case last cited, in these words: "Upon the general ground of reason and justice, no such answer can be set up. The defendants having had the benefit of the performance by the corporation of the several stipulations into which they entered, have received the consideration for their own promises; such promise by them is, therefore, not nudum pactum; they never can want to sue the corporation upon the contract in order to enforce the performance of their stipulations which have been already voluntarily performed, and therefore no sound reason can be suggested why they should justify their refusal to perform the stipulations made by them on the ground of inability of the corporation, which suit they can never want to sustain."

The same principle was adjudged in R. and B. R. Co. v. Proctor (29 Vt. 93), Ch. J. Redfield saying: "The only wrong in the directors is in having exceeded their powers; the transaction with the defendants, so far as it goes, will tend to restore a portion of the money to its rightful proprietor, and of this the defendants ought not to complain as they are confessedly solicitous to bring the directors of the plaintiff's company back to their legitimate

functions." (See, also, *Farmers' and Millers' Bank v. D. and M. R. Co.*, 17 Wis., 372.)

The same equitable principle was intimated by Ch. J. Kent, in *Silver Lake Bank v. North* (4 J. Ch., 370). *Parish v. Wheeler* (22 N. Y., 494), proceeds and was adjudged upon this general rule, Ch. J. Comstock, enunciating the doctrine that "the executed dealings of corporations must be allowed to stand for and against both parties, where the plainest rules of good faith require."

Palmer v. Lawrence (3 Sandf. Sup. Ct. R., 161), lays down the proposition in more comprehensive terms. Judge Duer, speaking for the court, says: "The general rule which is fairly deducible from all the cases on this subject is, that a defendant who has contracted with a corporation *de facto* is never permitted to allege any defect in its organization as affecting its capacity to contract or sue." The proposition may not be true in respect to contracts executory and wholly unexecuted; we do not pass upon that. It was decided in the *Steam Navigation Co. v. Weed* (17 Barb., 378), that when it was a simple question of capacity to contract arising either on a question of regularity of organization or of powers conferred by the charter, a party who has had the benefit of the contract cannot be permitted, in an action founded upon it, to question its validity. Judge Parker's opinion, to which nothing need be added, is well fortified by the many cases to which he refers and which, aside from the argument of the learned judge, abundantly sustain the judgment. Among the cases referred to and commented upon by Judge Parker, are *Silver Lake Bank v. North* (*supra*); *State of Indiana v. Woram* (6 Hill, 37); *Chester Glass Co. v. Dewey* (16 Mass., 94); *Steamboat Co., v. McCutcheon* (13 Penn. St. R., 13).

It is very evident, as well upon principle as upon authority, that had this action been against the debtor corporation the objection that the contract was not authorized by the charter of the plaintiff would have been untenable and the plaintiff would have been entitled to recover. * * *

When it is proved that the corporation has received property from others under a promise to pay, under circumstances which the law would adjudge sufficient to charge the corporation for the purchase-price, a debt is established which the trustees cannot dispute, although perchance the corporation might, for any reason, have refused to accept the property; and had it done so no legal liability would have resulted. * * *

² *Magee v. Pacific Improvement Co.* (1893) 98 Cal. 678, 33 Pac. 772; *Bradley v. Ballard* (1870) 55 Ill. 413; *Wright v. Hughes* (1889) 119 Ind. 324, 21 N. E. 907; *Prescott Nat. Bank v. Butler* (1893) 157 Mass. 548, 32 N. E. 909; *Seymour v. Chicago etc. Life Society* (1893) 54 Minn. 147, 55 N. W. 907; *Camden etc. R. Co. v. May's Landing etc. R. Co.* (1886) 48 N. J. Law 530, 7 Atl. 523; *Oil Creek etc. R. Co. v. Pennsylvania Transportation Co.* (1876) 83 Pa. St. 160; *Wright v. Pipe Line Co.* (1882) 101 Pa. St. 204; *Bond v. Terrell Cotton etc. Mfg. Co.* (1891) 82 Tex. 309, 18 S. W. 691;

BATH GAS LIGHT CO. v. CLAFFY.

1896. 151 N. Y. 24, 45 N. E. 390.¹³

APPEAL from a judgment of the General Term of the Supreme Court in the second judicial department, entered December 13, 1893, which affirmed a judgment in favor of plaintiff entered upon a decision of the court on trial at Circuit, a jury having been waived.

The nature of the action and the facts, so far as material, are stated in the opinions.

ANDREWS, Ch. J.—A brief statement of the material facts will present the important questions arising upon this appeal.

The plaintiff is a Maine corporation created under a special law of that state, passed in 1853, for the purpose of supplying gas for the lighting of the streets and buildings in the city of Bath. The United Gas, Fuel and Light Company is also a Maine corporation, organized in 1888, under a general law, by the executing and filing of a certificate, which in pursuance of the law of Maine was first submitted to and approved by the attorney-general, who certified that it was conformable to the Constitution and laws of that state. The certificate, among other things, specified that the corporation was organized to "manufacture, lease, purchase and otherwise acquire, deal in, manage, use and sell any and all machinery, fixtures, appurtenances, appliances and plants for using and furnishing light, heat and power, and for any and all purposes for which gas is now used." The plaintiff under its charter established a plant, and at the time of the execution of the lease now to be mentioned was engaged in supplying the streets and buildings in Bath with gas for lighting and other purposes. On the 10th day of November, 1888, it executed to the United Gas, Fuel and Light Company a lease of its property and franchises for the term of twenty-five years from November 1, 1888, at an annual rent of \$2,500, which the lessee covenanted to pay in semi-annual payments on the first day of May and the first day of November in each year, and also the taxes assessed during the term. Provision was made for the payment by the lessor to the lessee, at the expiration of the term, of the value of any improvements or extensions made by the lessee, and it was also provided that the lessee should give

McElroy v. Minnesota etc. Horse Co. (1897) 96 Wis. 317, 71 N. W. 652, *Accord*.

Plaintiff insured against damage by hail in a corporation authorized to insure "against loss or casualty by fire or lightning." A loss occurred. The corporation denied liability. *Held*, plaintiff could recover. *Denver Fire Ins. Co. v. McClelland* (1885) 9 Colo. 11, 9 Pac. 771. But see *Re Phoenix Life Assurance Co.* (1862) 2 Johns. & Hemm. 441; *Miller v. Insurance Co.* (1893) 92 Tenn. 167, 21 S. W. 39.—Eds.

¹³ Portions of prevailing opinion, and dissenting opinion of Vann, J., are omitted.—Eds.

to the lessor a satisfactory bond for the faithful performance by the lessee of its covenants in the lease. In pursuance of the provision last mentioned, the United Gas, Fuel and Light Company, on the same day, executed a bond with the defendants John Claffy and John T. Rowland as sureties, conditioned for the faithful performance by the company of the covenants in its behalf contained in the lease, which bond was delivered to and accepted by the plaintiff. The sureties were interested in the United Gas, Fuel and Light Company as stockholders, and Claffy (the appellant) was also a director. The lessee immediately, upon the execution of the lease, entered into possession of the demised property and paid the rent up to the 1st day of November, 1889, but defaulted in the semi-annual payment due May 1st, 1890, and on the 2nd day of August, 1890 (the rent remaining unpaid), the plaintiff re-entered and took possession of the demised property under a provision of the lease which authorized the lessor to enter and expel the lessee on failing to pay rent. The entry also was, as may be inferred, with the consent and, indeed, at the suggestion of the officers of the lessee. This action was brought on the bond against the lessee and the sureties to recover as damages the rent which fell due May 1, 1890, and the proportionate rent from that date up to August 2nd, 1890, and taxes which had been assessed against the property during its occupation by the lessee, which it had failed to pay.

The defendant Claffy alone appeared and defended the action. His sole defence to the general claim is that the lease was *ultra vires*, illegal and void, because (as is conceded) it was made without legislative sanction. If the court is compelled to accede to this contention by force of controlling authority, or from considerations of public policy which overbear in the particular case the rules of ordinary justice, it will be our duty so to declare and to say that, although the United Gas, Fuel and Light Company received and enjoyed the undisturbed possession of the demised property under the lease until the re-entry, and accepted and appropriated the benefit of the contract, nevertheless, when called upon to pay the rent which accrued during its occupation, it may defend itself on the ground that the plaintiff, in making the lease, exceeded its power and escape the performance of its obligation, and, further, that the defendant Claffy may, for a like reason, avoid his guaranty.

The modern doctrine, as stated by Chancellor Kent, is to consider corporations as having such powers as are specifically granted by the act of incorporation, or as are necessary for the purpose, of carrying into effect the powers expressly granted, and as not having any others. (2 Kent Comm. 299). This doctrine is embodied in the Revised Statutes of New York, and the section relating to the subject is regarded as simply declaratory of the antecedent law. (1 Rev. St. 600, § 3.) * * *

The modern and reasonable doctrine that contracts into which

corporations may lawfully enter are such only as are expressly or impliedly authorized by their charters, is nevertheless frequently disregarded in practice, and when this is done and a corporation enters into a contract beyond its chartered powers, the question arises which has been the subject of debate and of much difference of opinion, how shall such a contract be treated by the courts, and whether the contract can create any rights as between the parties which the courts will enforce. There are some propositions pertaining to the general subject which are beyond dispute. One is, that a contract by a corporation to do an immoral thing, or for any immoral purpose, or, to use a convenient expression, a contract *malum in se*, is void and gives no right of action. The doctrine, however, is not peculiar to contracts of corporations. It has its root in the universal principle that persons shall not stipulate for iniquity. Another principle of general recognition is that a corporation cannot enter into or bind itself by a contract which is expressly prohibited by its charter or by statute, and in the application of this principle it is immaterial that the contract, except for the prohibition, would be lawful. No one is permitted to justify an act which the legislature within its constitutional power has declared shall not be performed. The series of cases in this state, known as the *Utica* insurance cases, afford an apt illustration. It was held that the restraining acts which prohibited the exercise of banking powers, including the discount of paper, by other than banking corporations, rendered void securities taken on such discount by corporations not possessing banking powers, and this, although the object of the restraining laws seems to have been the protection of the chartered banks in the monopoly of banking.

But in not infrequent instances corporations enter into unauthorized contracts, which are neither *mala in se* nor *mala prohibita*, or when the only prohibition or restriction is implied from the grant of specified powers. It is this class of cases which open the field of controversy. Is such a contract performed by one party, but not performed by the other, void as between them to all intents and purposes, so that no recovery can be had under it against the party who has received the consideration for his promise, but neglects or refuses to perform it, or is it so tainted with illegality that the courts must refuse to recognize it under any circumstances or enforce its obligation, whether as to past or future transactions? There are certain English cases which are relied upon by those who maintain the strict view that contracts of corporations *ultra vires* are under no circumstances enforceable in the courts.

(The learned judge proceeded to discuss and distinguish the English decisions.)

The Supreme Court of the United States seems to be committed to a construction of the doctrine of *ultra vires* which would sustain the defense in the case now before us. Several cases have arisen in that court upon leases of railroads made without legislative

sanction, in which it has been held that such leases are void as between the parties, and that no action can be maintained thereon to recover the rent reserved, even during the occupation by the lessee under the lease.

(The learned judge then considered the leading Federal decisions.)

We concede that a railroad or other corporation invested with powers in the exercise of which the public have an interest, and empowered by reason of its quasi public character to do acts and exercise privileges peculiar and exceptional to enable it to discharge its public duties, cannot, as against the public, abdicate its functions or absolve itself from the performance of such duties through an unauthorized transfer of its property and franchises to another body or corporation. We have so held in the case of *Abbott v. The Johnstown, etc., Railroad Co.* (80 N. Y. 27), where it was decided that a railroad corporation which, without legal sanction, had leased its road, was not thereby exempted from liability as carrier to a passenger injured by negligence during the operation of the road under the lease.

There are obvious reasons of propriety and public policy, the prevention of monopolies, among others, aside from the mere question of capacity under their charters, which enforce the now well-settled doctrine, that leases by such quasi public corporations, to be valid and effectual, must be authorized by statute. But where, as in the present case, such an unauthorized lease has been made, and the lessee has received and enjoyed the possession of the property under the lease, is there any public policy which requires that the lessee should be permitted to escape the obligation imposed by the contract to pay the rent reserved during the enjoyment of the property? It is doubtless true, as has been suggested, that the corporation in such cases cannot, without the consent of the state, change its obligations to the state or the public, and discharge itself from its public duties. But the law affords ample remedy for the usurpation by corporations of unauthorized powers, through proceedings by injunction or for the forfeiture of their charters. If a lease by a corporation, made in excess of its powers and without legislative sanction, is illegal in the ordinary and proper sense of the term, it may be properly conceded that no action could be maintained upon it. The lessee, when sued for the rent, could set up the illegality of the contract, and the defense would prevail, however inequitable the defense might be. But the term "illegal", which is frequently used to describe a contract made by a corporation in excess of its corporate powers, in most cases means simply that the contract is unauthorized, or one which the corporation had no legal capacity to make. Such a contract may be illegal in the true and proper sense, but it may also be one involving no moral turpitude and offending against no express statute. The inexact and misleading use of the word "illegal", as applied to contracts of

corporations, ultra vires only, has been frequently alluded to. (Comstock, C. J., *Bissell v. M. S. Railroad Co.*, 22 N. Y. 268; Archibald, J., *Riche v. Ashbury Railway Carriage Co.*, L. R. [9 Exch.] 293; Lord Cairns, S. C. on appeal, L. R. [7 Eng. & Ir. App.] 672.)

The lease now in question was not in any true sense of the word illegal. It was undoubtedly void as against the state. The parties to the lease assumed it to be valid. It was contemplated, as the provisions of the lease show, that the lessee would continue and extend the business before carried on by the plaintiff, and it is not suggested that it did not, during its occupation, discharge all the obligations to the public which rested upon the plaintiff. The state has not intervened, and the possession of the property has now been restored to its original proprietors. The contract has been terminated as to the future, and all that remains undone is the payment by the lessee of the unpaid rent. We think the demands of public policy are fully satisfied by holding that, as to the public, the lease was void, but that, as between the parties, so long as the occupation under the lease continued, the lessee was bound to pay the rent, and that its recovery may be enforced by action on the covenant. Public policy is promoted by the discouragement of fraud and the maintenance of the obligation of contracts, and to permit a lessee of a corporation to escape the payment of rent by pleading the incapacity of the corporation to make the lease, although he has had the undisturbed enjoyment of the property, would be, we think, most inequitable and unjust. It has been suggested, to avoid the apparent injustice which would result from holding that there could be no recovery on the contract for past-due rent, that there might be a remedy on an implied contract to pay the value of the use of the property. But if the express contract was illegal in a proper sense, and the parties to the lease were guilty of a public wrong, so as to preclude a court of equity to entertain jurisdiction on the application of a lessor to be relieved from the lease and to be restored to the possession of the leased property, as was held in the case of *The St. Louis, V. & T. H. Railroad Co. v. Terre Haute & I. Railroad Co.* (145 U. S. 393), then surely it would be a mere evasion and would be inconsistent with legal principles for the court to imply a contract from the occupation under the illegal lease to relieve the wrongdoer from the dilemma into which he had voluntarily placed himself. We think the rule which should be applied is that the lessee is bound by the contract so long as he remains in possession.

It is unnecessary now to determine whether a lessee under an ultra vires lease may relieve himself from liability in the future by abandoning the possession and restoring, or offering to restore, it to the lessor.

The courts in this state from an early day, commencing as far back as the *Utica Insurance* cases, have sought to regulate and restrict the defense of ultra vires so as to make it consistent with

the obligations of justice. (*Utica Ins. Co. v. Scott*, 19 John. 1; *Curtis v. Leavitt*, 15 N. Y. 9; *Bissell v. M. S. Railroad Co.*, 22 id. 260, Op. Comstock, C. J.; *Parish v. Wheeler*, Id. 495; *Whitney Arms. Co. v. Barlow*, 63 id. 62; *Pratt v. Short*, 79 id. 437; *Woodruff v. Erie Railway Co.*, 93 id. 609; *Starin v. Edson*, 112 id. 206.) The case of *Woodruff v. Erie Railway* (*supra*) is very much in point in the present controversy. It was there held that the lessee of a railroad could not resist the payment of rent which accrued during its occupation under the lease on the ground that the lessor's title was derived under an *ultra vires* transaction. Our conclusion, therefore, is that the main question was properly decided against the defendant. It is said, however, that the contract was a Maine contract, and that by the law of that state the lease was illegal and void and no action could be maintained upon it. It is a sufficient answer to this claim that the law of Maine on the subject does not appear by the record, and that it is the duty of this court, therefore, to determine the case according to the law of New York as established, or in the absence of controlling authority, as justice having regard to all interests may seem to the court to require.

The question as to the liability of the defendant for the taxes assessed in 1890 was, we think, correctly adjudged.

Finding no error in the record the judgment should be affirmed.

All concur with Andrews, Ch. J., except Vann, J., dissenting.

Judgment *affirmed*.

VISALIA GAS, ETC., LIGHT CO. v. SIMS.

1894. 104 Cal. 326, 37 Pac. 1042.¹⁴

Plaintiff, incorporated to furnish gas and electricity to the inhabitants of Visalia, leased its plant and business to one Lynch for the term of two years from June 1, 1887, in consideration of Lynch's covenanting to pay to plaintiff the entire net receipts of said business and further guaranteeing that the amounts so paid should be sufficient to enable plaintiff to pay an annual dividend to its stockholders of 5 per cent. upon its capital stock of \$28,000. The defendants became sureties for Lynch. Lynch took possession of the demised property and retained it until June 1, 1889, without paying plaintiff any sums as rental, the receipts from the property being insufficient to pay running expenses. This action is to recover the sum of \$2,800, alleged to be due plaintiff under the suretyship agreement.

TEMPLE, C.— * * *

The main defense, however, is that the lease is *ultra vires* and against public policy.

¹⁴ Statement rewritten. Portion of opinion omitted.—Eds.

The real question presented is not that the lease is ultra vires as to the corporation, but that plaintiff having availed itself of the franchise granted it by the city of Visalia, it became its legal duty to operate its gas and electric works, and to supply the inhabitants with gas and electricity, and it was, therefore, against public policy to lease those works and privileges to Lynch, and thus disable itself for the time from performing its duty.

This proposition is clearly maintained in *Thomas v. Railroad Co.*, 101 U. S. 71. That was the case of a lease of a railroad and franchise. The court said, speaking through Mr. Justice Miller:

"Where a corporation like a railroad company has granted to it by charter a franchise intended in large measure to be exercised for the public good, the due performance of those functions being the consideration of the public grant, any contract which disables the corporation from performing those functions, which undertakes, without the consent of the state, to transfer to others the rights and powers conferred by the charter, and to relieve the grantees of the burden which it imposes, is a violation of the contract with the state, and is void as against public policy. This doctrine is asserted with remarkable clearness in the opinion of this court, delivered by Mr. Justice Campbell, in *York etc. R. R. Co. v. Winans*, 17 How. 30. * * *

"This conclusion [argument] implies that the duties imposed upon the plaintiff by the charter are fulfilled by the construction of the road, and that by alienating its right to use, and its powers of control and supervision, it may avoid further responsibility. But those acts involve an overturn of the relations which the charter has arranged between the corporation and the community. Important franchises were conferred upon the corporation to enable it to provide facilities for communication and intercourse required for the public convenience. Corporate management and control over these were prescribed, and corporate responsibility for their insufficiency provided as a remuneration to the community for their grant. The corporation cannot absolve itself from the performance of its obligations without the consent of the legislature."

* * * * *

It is said, however, that when a contract which was ultra vires has been performed on one part, the other is then estopped to plead that the contract was ultra vires. Here, however, the contract was void, because against public policy. In such cases courts will not give relief to either party.

Respondent contends that the rule is different as to corporations, and some cases seem to sustain the claim. It is impossible to see why there should be a difference in such cases because one party is a corporation. It is sometimes said, however, that a contract of a corporation is against public policy when it is simply ultra vires, because it is against public policy that a corporation should assume to exercise powers not granted. In such case it is simply

an executed ultra vires contract. But it may also be an attempt to do that which is unlawful without reference to the corporate franchise, a contract which would be unlawful in a natural person. In such case the contract of the corporation is subject to the same rule which obtains in the case of individuals.

But it would make no difference here. The lessee, it is found, made nothing from the lease. The rule is the same that it would have been had the corporation been sued.

Says Morawetz on Private Corporations, section 715: "If money or property is given to a corporation under a contract which is void because the agent assuming to represent the corporation in the transaction had no authority to bind it, the corporation is liable to account for the money or other property received. * * * Thus in *Burges and Stocks* case, 2 Johns. & H. 441, the directors of a life assurance company had issued policies of marine insurance, and applied the premiums to the use of the company. Upon winding up the company the holders of the policies were held not to be entitled to prove for losses, but were allowed the amount of the premiums paid. Vice-Chancellor Page-Wood said: 'They had no consideration for the premiums they paid. The directors, it is true, had no power to issue marine policies, but they had power to receive money, and apply it for the benefit of the company. It is proved that they did so receive and apply these premiums, and the amount might have been recovered even at law as money had and received.'"

So, he says, a corporation cannot be charged with a loan of money made by its directors without authority, but, if any portion of the money has been applied to the proper uses of the company, it may be held liable to that extent at least. It is said: "The liability of the company does not, in such case, arise from the contract entered into by the directors, but from the equitable right of the lender to recover his money, which has gone to swell the company's assets."

I think this is the principle which underlies most of the cases upon this subject, although forced to admit that some are not consistent with it.

This action is on the contract to recover an amount of money which the lessee guaranteed the property would pay, but which it did not. It is not for any amount of benefit which he received from the contract. It is found that he received no benefit upon it. The fact that there was a consideration which would prevent the contract from being a nudum pactum for the want of it does not make a case of benefits to be paid for, where a contract is ultra vires. And the contract being against public policy should not be enforced.

I recommend that the judgment be set aside and judgment on the findings ordered for defendants.

HAYNES, C., and SEARLS, C., concurred.

For the reasons given in the foregoing opinion, the judgment is

set aside, and judgment on the findings ordered for defendants.
 GAROUTTE, J., HARRISON, J., VAN FLEET, J.
*Hearing in Bank denied.*¹⁵

APPLETON v. CITIZENS' CENTRAL NAT. BANK.

1908. 190 N. Y. 417, 83 N. E. 470.

CITIZEN'S CENTRAL NAT. BANK v. APPLETON.

1909. 216 U. S. 196, 54 L. ed. 443.

APPEAL from a judgment entered June 1, 1907, upon an order of the Appellate Division of the Supreme Court in the first judicial department which affirmed a judgment of Special Term sustaining a demurrer to and directing a dismissal of the complaint.

The nature of the action and the facts, so far as material, are stated in the opinion.

CULLEN, Ch. J.—This action is brought by the plaintiff as receiver of a dissolved bank against the defendant, who is the successor of the Central National Bank of the city of New York. The complaint which thus far has been held not to state a good cause of action alleges that on the 4th day of January, 1904, the bank which the plaintiff represents loaned and advanced to one Mikael Samuels the sum of \$12,000 on the written agreement of said Samuels to repay said sum on or before four months after date with interest, the repayment of which said loan the Central National Bank guaranteed by the following instrument: "For and in consideration of one dollar and other good and valuable considerations, the Central National Bank of the City of New York hereby guarantees to the Cooper Exchange Bank the payment at maturity of a loan of twelve thousand dollars, made this day to Mikael Samuels & Co., by the Cooper Exchange Bank;" that at the time of said loan said Samuels was indebted to said Central Bank in the sum of \$10,000; that said loan was obtained by said Samuels and guaranteed by said Central Bank for the purpose and upon the agreement that the said Central Bank should receive out of said loan the sum of said \$10,000, which Samuels owed to it, which said sum said Central Bank did receive from Samuels; that Samuels failed to pay said loan except the sum of \$1,000. Judgment is demanded for the remaining sum of \$11,000 and interest. The Appellate Division decided the case by a di-

¹⁵ See also *Twiss v. Guaranty Life Assn.* (1893) 87 Ia. 733, 55 N. W. 8; *Sturdevant v. Farmers & Merchants Bank* (1901) 62 Neb. 472, 87 N. W. 156; *Jemison v. Citizens' Savings Bank* (1890) 122 N. Y. 135, 25 N. E. 264; *Gause v. Commonwealth Trust Co.* (1909) 196 N. Y. 134, 89 N. E. 476 ("The plaintiff has never given to the defendant any concrete thing by virtue of the agreement"); *Deaton Grocery Co. v. International Harvester Co.* (1907) 47 Tex. Civ. App. 267, 105 S. W. 556.—Eds.

vided court on the authority of a decision on a previous appeal. The complaint now before us is an amended one and the record does not contain the original complaint, consequently we are not informed as to what difference exists between the allegations of the two pleadings.

The plaintiff has been defeated on the theory that the execution of the guaranty by the defendant bank was ultra vires and not binding upon it, and upon this ground the judgments below are sought to be sustained. Had the guaranty been limited to the amount which the bank, under its agreement with Samuels, was to receive out of the loan, we should be entirely clear that it was within the legitimate powers of the bank under the decisions of the Supreme Court of the United States in *People's Bank v. National Bank* (101 U. S. 181) and *Cochrane v. United States* (157 U. S. 286). It was there held that a contract of guarantee of paper held by it was within the implied powers of a national bank, and this though, as in the later of the cases cited, the note was not made to the guaranteeing bank, but directly to the order of another bank to which the guaranty was made. We think, however, that the defendant's power to guarantee was limited by the extent of its interest in the subject-matter of the guaranty. To allow a bank to guarantee the payment by one of its debtors of a larger sum in order that the bank might receive or retrieve a lesser sum would be to permit it to enter upon very hazardous speculation and authorize very wild and unsafe banking. The learned counsel for the appellant frankly conceded on the argument that a recovery should be limited to the amount received by the defendant. It is insisted, however, that the contract of guaranty must be deemed either good or bad as an entirety, and cannot be upheld in part and rejected in part. I am not willing to concede this claim, but it is unnecessary to discuss it, for its determination is not necessary to the decision of the case. We may assume that the contract was ultra vires. We may further assume that in transactions by national banks we should adopt the law of ultra vires as it prevails in the Federal courts, and not the local law on the subject. Yet the defendant, in our opinion, became plainly liable for the amount which it received under the ultra vires contract. The law which obtains in this state and in several other jurisdictions is that where one party has received the full benefit of an ultra vires contract it cannot plead the invalidity of the contract to defeat an action upon it by the other party. (*Bath Gas Light Co. v. Claffy*, 151 N. Y. 24.) A contrary rule obtains in the Supreme Court of the United States. There it is held that the execution of an ultra vires contract by one party cannot confer upon it validity or authorize the other party to sue on its obligations (*Central Transportation Company v. Pullman Palace Car Co.*, 139 U. S. 24), but at the same time it is also held that a party cannot retain money or property received by it under an ultra vires contract when it refuses to perform that contract. (*Logan County Bank v. Townsend*, 139 U. S. 67.) It was there

said by Judge Harlan: "The bank, in this case, insisting that it obtained the bonds of the plaintiff in violation of the act of Congress, is bound, upon being made whole, to return them to him. No exemption or immunity from this principle of right and duty is given by the national banking act. 'The obligation to do justice,' this court said in *Marsh v. Fulton County* (10 Wall. 676, 684), 'rests upon all persons, natural and artificial, and if a county obtains the money or property of others without authority, the law, independently of any statute, will compel restitution or compensation.'" In a great many cases the difference between the law prevailing in the Federal courts and that in our own would lead to great difference in results. In this case, however, as the plaintiff disclaims any right to recover beyond the amount actually received by the defendant, the result is exactly the same whether we adopt one rule or the other. Whatever the difference of view there may be as to the effect of ultra vires on corporate contracts, in no jurisdiction can a party retain what it has received under such a contract and refuse to perform the contract.

It is urged by the counsel for the respondent that payment by its debtor of the claim it held against him constituted no consideration for the guaranty, for the debtor was bound to perform his obligation. There is no force in this suggestion. The money the defendant received was not that of Samuels, but the plaintiff's, and Samuels was merely the conduit through which it was paid to the defendant. It is not a question of consideration between Samuels and the plaintiff, but of consideration between the plaintiff and the defendant. The plaintiff parted with its money solely on the guaranty of the defendant. (Whoever heard that the loan of money to the principal was not sufficient consideration for the obligation of the surety?) In this case it was the surety who got the money.

Nor is there any force in the suggestion that this action is not brought in disaffirmance of the contract for money had and received but on the contract of guaranty. All the facts are set forth in the complaint, and if these facts entitle the plaintiff to relief on any theory, then the complaint states a good cause of action.

The judgments of the Appellate Division and Special Term should be reversed and judgment rendered for plaintiff on demurrer, with costs in all the courts, with leave, however, to the defendant, within twenty days, to withdraw demurrer and serve answer upon the payment of such costs.

GRAY, HAIGHT, WERNER, WILLARD BARTLETT and HISCOCK, JJ., concur; EDWARD T. BARTLETT, J., taking no part.

Judgment accordingly.

The case was remitted to the Supreme Court of New York and judgment was there rendered against defendant for \$10,000, with interest from January 4, 1904, with costs in all courts. Defendant brought the case on writ of error to the Supreme Court of the United States.

MR. JUSTICE HARLAN. * * *

The plaintiff in error insists that the guaranty given by the Central National Bank to the Cooper Exchange Bank was beyond its power, was in violation of the National Banking Act, and, therefore, could not be made the foundation of an action against the guarantor bank. But this action need not be regarded as one on the written contract of guaranty, but as based on an implied contract between the Cooper Exchange Bank and the Central National Bank, whereby the latter, under the circumstances disclosed by the record, came under a duty to account to the former for the \$10,000 of the \$12,000 actually paid to Samuels at its request and on its guaranty. The law would be very impotent to do justice if it could not, under those circumstances and without violating established legal principles, compel the Central National Bank to recognize and discharge that duty. Samuels owed the Central National Bank \$10,000, and—with knowledge perhaps of his financial condition—he was put forward by that bank to obtain \$12,000 from the Cooper Exchange Bank so that it could get \$10,000 out of that sum, for its own use. The circumstances show that the latter bank would not have loaned the money to Samuels except at the request and on the guaranty of the Central National Bank. All this, it may be observed, occurred under a previous agreement between the Central National Bank and Samuels, that that bank was to have \$10,000 of the \$12,000 in discharge of its claim upon him. In short, the Central National Bank, by means of the device mentioned, got \$10,000 of the money of the Cooper Exchange Bank for its own use, and having used it for its own benefit, it now seeks to avoid liability therefor, upon the ground that it was not allowed by the law of its creation to execute the guaranty in question. We know of no adjudged case that stands in the way of relief being granted as asked by the plaintiff. But there are many that will authorize such relief.

(The learned justice proceeded to review the authorities.)

We need not go farther. It is entirely clear that the judgment against the defendant bank—which came into the possession of the property, and was subject to the liabilities of the Central National Bank—was consistent with sound legal principles and was intrinsically right, even if the guaranty in question was beyond the power of the guaranteeing bank, under the national banking statutes. Whatever may be said as to the validity of the written guaranty, now alleged to be illegal, the judgment can be supported as based wholly on the implied contract, which made it the duty of the Central National Bank, under the facts disclosed, to account to the Cooper Exchange Bank for the money obtained from the latter in execution of the agreement made by the former with the borrower.

The judgment must be affirmed.

It is so ordered.¹⁶

*Based
on ground
implied
to return
the money.*

¹⁶ Rankin v. Emigh (1910) 218 U. S. 27, Accord.

LONG v. GEO. PACIFIC R. CO.

1890. 91 Ala. 519, 8 So. 706.¹⁷

McCLELLAN, J.—The case made by the amended bill is this: On April 23, 1883, the complainant, B. M. Long, and his wife, Amanda C. Long, executed to the Georgia Pacific Railway Co. a deed upon valuable consideration presently paid, to and of the iron, coal and oil interests and properties in and pertaining to certain tracts of land, aggregating about four thousand acres; the said Long retaining the fee to said lands, except in respect to said mineral interests, and continuing in possession thereof. The grantee is a corporation, and was and is without power to purchase and hold said land, or the mineral interests in the same. The bill seeks to have the deed declared void, because of this incapacity of the corporation, and to have the same cancelled as a cloud upon complainant's title. The bill was demurred to on several grounds, and the demurrer was sustained generally, the decree to that end being now assigned as error.

Only those grounds of error which present the question, whether a vendor who has sold, received payment for, and conveyed land to a corporation, which had no power to hold the same, can have any relief in respect to the transaction, are discussed in argument; and to these our consideration will be confined, since it is manifest that the determination of this question, in line with the decree below, as we think it must be determined, will be fatal, not only to the present appeal, but to complainant's cause of action.

It is thoroughly well settled law, that a party to an *ultra vires* executory contract made with a corporation is not estopped to set up the want of corporate capacity in the premises, either by the fact of contracting, whereby the power to contract is, in a sense, admitted or recognized, or by the fact that the fruits or issues of the contract have been received and enjoyed; and this, though the assault upon the transaction comes from the corporation itself—*Marion Savings Bank v. Dunklin*, 54 Ala. 471; *Chambers v. Falkner*, 65 Ala. 448; *Sherwood v. Alvis*, 83 Ala. 115; *Chewacla Lime Works v. Dismukes*, 87 Ala. 344. But, where the contract is fully executed—where whatever was contracted to be done on either hand has been done—a different rule prevails. In such case, the law will not interfere, at the instance of either party, to undo that which it was originally unlawful to do, and to the doing of which, so long as the contract to that end remained executory, neither party could have coerced the other. As declared by Mr. Bishop, "the parties voluntarily doing of what they have unlawfully agreed, places them, in effect, in the same position as if the contract had been originally good; neither can recover of the other what was parted with. The

¹⁷ Statement omitted.—Eds.

'reason for which is, that, since they are equally in fault, the law will help neither.'—Bishop on Contracts, § 627.

The former decisions of this court are in line with this doctrine, and fully recognize the distinction between executory and executed void contracts, to the effect that, while suits to enforce the former may always be defended on the ground of their invalidity, no relief prayed upon such ground can be granted with respect to the latter.

—*Morris v. Hale*, 41 Ala. 510; *Ingersoll v. Campbell*, 46 Ala. 282; *Sherwood v. Alvis*, 83 Ala. 115; *Dudley v. Collier*, 87 Ala. 431; *Craddock v. Mortgage Co.*, 88 Ala. 281. And this is the doctrine generally declared by other courts—*Thomas v. Railroad Co.*, 101 U. S. 71; *Day v. S. S. B. Co.*, 57 Mich. 146; s. c. 52 Amer. Rep. 352; *Parish v. Wheeler*, 22 N. Y. 494; *Miners' Ditch Co. v. Tellerbach*, 37 Cal. 542, 606; *Terry v. Eagle Lock Co.*, 47 Conn. 141.

There is no question but that the case presented by the bill involved a contract on the part of the railway company to buy, and on the part of the complainant to sell, certain interests in the land described. It is equally clear that the payment of the agreed price on the one hand, and the execution of the conveyance on the other, fully executed this contract on both sides, left nothing to be done by either party in the premises, and bring the transaction within the principle we have been considering, which denies to the complainant any relief in respect to it.

The same conclusion is reached by another well established principle. It is, that when a party sells and conveys property to a corporation, which is without power to purchase and hold the same, and receives compensation therefor, there being no fraud in the transaction, he is in no sense injured or prejudiced by the incapacity of the corporation, nor can he be heard to complain of it; but the question becomes one between the corporation and the State, the sovereign alone having the right to impeach the transaction; and until it supervenes for this purpose, the corporation is vested with perfect title against all the world, defeasible only on office found.—*R. & B. Railroad Co. v. Proctor*, 29 Vt. 93; *Leazure v. Hillegas*, 7 Serg. & Rawle, 313; *Goundie v. Northampton Water Co.*, 7 Pa. St. 233; *Baird v. Bank of Washington*, 11 Serg. & Rawle, 411; *Lathrop v. Bank*, 8 Dana, 114, 129; *Hough v. Cook County Land Co.*, 73 Ill. 23; s. c., 24 Amer. Rep. 230; *Cowles v. Springs Co.*, 100 U. S. 55; *Reynolds v. Crawfordsville Bank*, 112 U. S. 405, 413; 2 Mor. Corp. § 710. *Affirmed.*¹⁸

¹⁸ *Hough v. Cook County Land Co.* (1874) 73 Ill. 23; *Hagerstown etc. Improvement Co. v. Keedy* (1900) 91 Md. 430, 46 Atl. 965; *City of Spokane v. Amsterdam Trustees Kantoor* (1900) 22 Wash. 172, 60 Pac. 141, *Accord*. —Eds.

ST. LOUIS, VANDALIA & TERRE-HAUTE R. CO. v. TERRE-HAUTE & INDIANAPOLIS R. CO.

1891. 145 U. S. 393, 36 L. ed. 738.¹⁹

THIS was a bill in equity filed by plaintiff, an Illinois corporation, to set aside and cancel a conveyance by way of lease, to the defendant, an Indiana corporation, of plaintiff's railroad, property and franchises, for the term of nine hundred and ninety-nine years. A demurrer to the bill was sustained below (33 Fed. 440). Further facts appear in the opinion.

MR. JUSTICE GRAY, after stating the case as above, delivered the opinion of the court.

The object of this suit between two railroad corporations, as stated in the amended bill, is to have a contract, by which the plaintiff transferred its railroad and equipment, as well as its franchise to maintain and operate the road, to the defendant for a term of nine hundred and ninety-nine years, set aside and cancelled, as beyond the corporate powers of one or both of the parties.

The contract, dated February 10, 1868, recites that the plaintiff is a corporation of Illinois, and the defendant a corporation of Indiana; that their railroads connect at the line between the two States; that it is desirable that the two roads should be operated by the defendant as one road; and that the defendant has "proposed to lease and operate" the plaintiff's road for a period of nine hundred and ninety-nine years. "It is therefore agreed" that, upon the completion of the plaintiff's road to the state line, the defendant "shall take charge of and operate the same with its equipment" for that period, and "shall be allowed sixty-five per cent of the gross receipts from all traffic moved over the line, or business done thereon, and from the property of the company, as a consideration for working and maintenance expenses," and shall appropriate the rest of such receipts to the payment of interest on the plaintiff's mortgage bonds, and pay any surplus to the plaintiff, for the benefit of its stockholders. Within a year afterwards, the contract was modified by providing that the defendant should be allowed seventy (instead of sixty-five) per cent of the gross receipts, "but if the working and maintenance expenses of said road shall be less than seventy per cent of the gross receipts aforesaid, then all of such excess shall be paid over to the" plaintiff. It is further agreed in the contract that the defendant "shall enjoy all the rights, powers and privileges of the" plaintiff, "so far as the same may be needful to maintain and operate said railroad," and may "impose and collect tolls and rates for transportation, and do all other acts and things, as fully and as effectually as the" plaintiff "could do if operating said line."

In short, by this contract one railroad corporation undertook to

¹⁹ Statement abridged. Portion of opinion omitted.—Eds.

transfer its whole railroad and equipment, and its privilege and franchise to maintain and operate the road, to another railroad corporation for a term of nine hundred and ninety-nine years, in consideration of the payment from time to time by the latter to the former of a certain portion of the gross receipts. This was, in substance and effect, a lease of the railroad and franchise for a term of almost a thousand years, and was a contract which neither corporation had the lawful power to enter into, unless expressly authorized by the State which created it, and which, if beyond the scope of the lawful powers of either corporation, was unlawful and wholly void, could not be ratified or validated by either or both, and would support no action or suit by either against the other. *Thomas v. Railroad Co.*, 101 U. S. 71; *Pennsylvania Railroad v. St. Louis, Alton & Terre Haute Railroad*, 118 U. S. 290, 630; *Oregon Railway v. Oregonian Railway*, 130 U. S. 1; *Central Transportation Co. v. Pullman's Car Co.*, 139 U. S. 24.

Upon the question whether this contract was ultra vires of either corporation, this case cannot be distinguished in principle from *Pennsylvania Railroad v. St. Louis, Alton & Terre Haute Railroad*, above cited.

(The learned judge proceeded to consider this question.)

It may therefore be assumed, as contended by the plaintiff, that the contract in question was ultra vires of the defendant, and therefore did not bind either party, and neither party could have maintained a suit upon it, at law or in equity, against the other.

It does not, however, follow that this suit to set aside and cancel the contract can be maintained. If it can, it is somewhat remarkable that, in the repeated and full discussions which the doctrine of ultra vires has undergone in the English courts within the last fifty years, no attempt has been made to bring a suit like this. The only cases cited in the elaborate briefs for the plaintiff, or which have come to our notice, approaching this in their circumstances, are in American courts not of last resort, and present no sufficient reasons for maintaining this suit. *Auburn Academy v. Strong, Hopkins* Ch. 278; *Atlantic & Pacific Telegraph Co. v. Union Pacific Railway*, 1 McCrary, 541; *Western Union Telegraph Co. v. St. Joseph & Western Railway*, 1 McCrary, 565; *Union Bridge Co. v. Troy & Lansingburgh Railroad*, 7 Lansing, 240; *New Castle Railway v. Simpson*, 21 Fed. Rep. 533.

The English cases relied on by the plaintiff were either suits to set aside marriage brokerage bonds, as in *Drury v. Hooke*, 1 Vernon, 412, and *Smith v. Bruning*, 2 Vernon, 392; S. C. nom. *Goldsmith v. Bruning*, 1 Eq. Cas. Ab. 89; or to recover back money paid for the purchase, without leave of the Crown, of a commission in the military or naval service, as in *Morris v. McCulloch, Ambler*, 433; S. C. 2 Eden, 190. Those cases have sometimes been justified upon the ground that, the agreement being against the policy of the law, the relief was given to the public through the party. *Debenham v. Ox*,

1 Ves. Sen. 276; *St. John v. St. John*, 11 Ves. 526, 536; *Cone v. Russell*, 3 Dickinson (48 N. J. Eq.) 208. But Sir William Grant explained them as proceeding upon the ground that the plaintiff was less guilty than the defendant. *Osborne v. Williams*, 18 Ves. 379, 382. And *Morris v. McCulloch* can hardly be reconciled with his decision in *Thomas v. Thomson*, 7 Ves. 470, or with the current of later authorities.

The general rule, in equity, as at law, is *In pari delicto potior est conditio defendentis*; and therefore neither party to an illegal contract will be aided by the court, whether to enforce it or to set it aside. If the contract is illegal, affirmative relief against it will not be granted, at law or in equity, unless the contract remains executory, or unless the parties are considered not in equal fault, as where the law violated is intended for the coercion of the one party and the protection of the other, or where there has been fraud or oppression on the part of the defendant. *Thomas v. Richmond*, 12 Wall. 349, 355; *Spring Co. v. Knowlton*, 103 U. S. 49; *Story Eq. Jur.* § 298.

While an unlawful contract, the parties to which are in *pari delicto*, remains executory, its invalidity is a defence in a court of law; and a court of equity will order its cancellation only as an equitable mode of making that defence effectual, and when necessary for that purpose. *Adams on Eq.* 175. Consequently, it is well settled, at the present day, that a court of equity will not entertain jurisdiction to order an instrument to be delivered up and cancelled, upon the ground of illegality appearing on its face, and when, therefore, there is no danger that the lapse of time may deprive the party to be charged upon it of his means of defence. *Story Eq. Jur.* § 700 a, and cases cited; *Simpson v. Howden*, 3 Myl. & Cr. 97; *Ayerst v. Jenkins*, L. R. 16 Eq. 275, 282.

When the parties are in *pari delicto*, and the contract has been fully executed on the part of the plaintiff, by the conveyance of property, or by the payment of money, and has not been repudiated by the defendant, it is now equally well settled that neither a court of law nor a court of equity will assist the plaintiff to recover back the property conveyed or money paid under the contract. *Thomas v. Richmond*, above cited; *Ayerst v. Jenkins*, L. R. 16 Eq. 275, 284. For instance, property conveyed pursuant to a contract made in consideration of the compounding of a crime, and the stifling of a criminal prosecution, and therefore clearly illegal, cannot be recovered back at law, nor the conveyance set aside in equity, unless obtained by such fraud or oppression on the part of the grantee, that the conveyance cannot be considered the voluntary act of the grantor. *Worcester v. Eaton*, 11 Mass. 368, and 13 Mass. 371; *Atwood v. Fisk*, 101 Mass. 363; *Bryant v. Peck & Whipple Co.*, 154 Mass. 460; *Williams v. Bayley*, L. R. 1 H. L. 200; *Jones v. Merionethshire Society*, 1892, 1 Ch. 173, 182, 185, 187.

In the case at bar, the contract by which the plaintiff conveyed its railroad and franchise to the defendant for a term of nine hundred

and ninety-nine years was beyond the defendant's corporate powers, and therefore unlawful and void, of which the plaintiff was bound to take notice. The plaintiff stood in the position of alienating the powers which it had received from the State, and the duties which it owed to the public, to another corporation, which it knew had no lawful capacity to exercise those powers or to perform those duties. If, as the plaintiff contends, the contract was also beyond its own corporate powers, it is certainly in no better position. In either aspect of the case, the plaintiff was in *pari delicto* with the defendant. The invalidity of the contract, in view of the laws of which both parties were bound to take notice, was apparent on its face. The contract has been fully executed on the part of the plaintiff by the actual transfer of its railroad and franchise to the defendant; and the defendant has held the property, and paid the stipulated consideration from time to time, for seventeen years, and has taken no steps to rescind or repudiate the contract.

Upon this state of facts, for the reasons above stated, the plaintiff, considered as a party to the unlawful contract, has no right to invoke the assistance of a court of equity to set it aside. And so far as the plaintiff corporation can be considered as representing the stockholders, and seeking to protect their interests, it and they are barred by laches. *Harwood v. Railroad Co.*, 17 Wall. 78; *Graham v. Birkhead & Co. Railway*, 2 Hall & Twells, 450; S. C. 2 Macn. & Gord. 146; *Ffooks v. Southwestern Railway*, 1 Sm. & Gif. 142, 164; *Gregory v. Patchett*, 11 Law Times (N. S.) 357.

This case is not like those in which the defendant, having abandoned or refused to perform the unlawful contract, has been held liable to the plaintiff, as upon an implied contract, for the value of what it had received from him and had no right to retain. *Spring Co. v. Knowlton*, 103 U. S. 49; *Logan County Bank v. Townsend*, 139 U. S. 67, and cases there cited.

But the case is one in which, in the words of Mr. JUSTICE MILLER, in a case often cited in this opinion, the court will not disturb the possession of the property that has passed under the contract, but will refuse to interfere as the matter stands. *Pennsylvania Railroad v. St. Louis, Alton & Terre Haute Railroad*, 118 U. S. 290, 316, 317. See also *Union Trust Co. v. Illinois Midland Co.*, 117 U. S. 434, 468, 469; *Central Transportation Co. v. Pullman's Car Co.*, 139 U. S. 24, 56, 57, 61.

*Decree affirmed.*²⁰

²⁰ See *Harriman v. Northern Securities Co.* (1904) 197 U. S. 244, especially pp. 295-6, 49 L. Ed. 739, 25 Sup. Ct. 493. But see *White v. President etc. of Franklin Bank* (1839) 22 Pick. (Mass.) 181: "This action proceeds in disaffirmance of an executory illegal contract, and was commenced before the money which the defendants contracted to pay, was by the terms of the contract payable; the plaintiff therefore had a right to rescind the contract or rather to treat it as a void contract, and to recover back the consideration money." See also *Newcastle etc. R. Co. v. Simpson* (1884) 21 Fed. 533.

NORTHWESTERN UNION PACKET CO. v. SHAW (1875) 37 Wis. 655. Action

PULLMAN'S PALACE CAR CO. v. CENTRAL TRANSPORTATION CO.

1897. 171 U. S. 138, 43 L. ed. 108, 18 Sup. Ct. 808.²¹

THE record in this case shows that in 1870 the Central Transportation Company, hereafter called the Central Company, was a corporation which had been in 1862 incorporated under the general manufacturing laws of the State of Pennsylvania. It was engaged in the business of operating railway sleeping cars and of hiring them to railroad companies under written contracts by which the cars were to be used by the railroad companies for the purpose of furnishing sleeping conveniences to travellers. The corporation at this time had contracts with a number of different railroad companies in the East, principally, but not exclusively, with what is known as the Pennsylvania Railroad system, and it had been engaged in its business with those companies for some time prior to 1870. In the year last named the Pullman's Palace Car Company, hereafter called the Pullman Company, was a corporation which had been incorporated under the laws of the State of Illinois. It was doing the same

by corporation engaged in business of common carrier upon contract for the sale of wheat to be delivered into plaintiff's barge. Judgment was demanded for \$1,000 paid on account, and for damages for breach of contract. *Held*, plaintiff not entitled to damages, but entitled to return of the \$1,000 advanced.

Page 661: " * * * when money has been paid upon an executory agreement, which is free from moral turpitude, and is not prohibited by positive law, but which is invalid by reason of the legal incapacity of a party thereto, otherwise capable of contracting, to enter into that particular agreement, * * * the money so paid may, while the agreement remains executory, be recovered back by the party paying it, in an action for money had and received."

MCCUTCHEON v. MERZ CAPSULE CO. (1896) 71 Fed. 787, 19 C. C. A. 108. Two corporations and two partnerships, all being engaged in manufacturing the same goods, entered into an agreement providing for the formation of another corporation to take over the property and business of the parties in interest and manufacture the goods, the stock of the new corporation to be allotted to the several parties in interest in agreed proportions, and bonds of the new company to be issued to them in payment for their property. One of the corporations, Merz Capsule Co., deciding to withdraw, tendered back the stock which it had received and demanded a rescission of the agreement. This was refused and the new corporation attempted to get possession of the property of the Merz Capsule Co. by force. The Merz Capsule Co. thereupon filed a bill praying for the cancellation of the agreement and for an injunction.

Held, that the agreement by which the Merz Capsule Co. was to abandon the exercise of its corporate powers and restrict itself to the holding of stock of another corporation was *ultra vires* and void;

Held, further, that the agreement being still in large part executory, the possession of the property not having been delivered to the new company and the bonds not having been delivered in payment, the Merz Capsule Co. was entitled to a decree cancelling the agreement and restraining the new company from interfering with the possession of its property.—Eds.

²¹ Statement abridged. Portions of opinion omitted.—Eds.

in action
C. Co. gave back the stock
to the new Co.
and 6 took a lease
new Co. for 2
years. After
case they as
at factory. 6
collected and
new Co. got
up. 2 d. 7
to separate
and publish
C. cancelled.
The factors
and Secors
were keeping
set back
N.

general kind of business in the West that the Central Company was doing in the East. For reasons not material to detail, the two companies entered into an agreement of lease, which was executed February 17, 1870.

By its terms the Central Company leased to the Pullman Company its entire plant and personal property together with its contracts which it had with railroad companies for the use of its sleeping cars on their roads, and also the patents belonging to it. The lease was to run for ninety-nine years, which was the duration of the charter of the Central Company.

It was also agreed that the Central Company would not engage in the business of manufacturing, using or hiring sleeping cars while the contract remained in force.

In consideration of these various obligations, the Pullman Company agreed to pay annually the sum of \$264,000 during the entire term of ninety-nine years, in quarterly payments, the first quarter's payment to be made on the first of April, 1870.

From the time of the execution of the contract its terms were carried out, and no particular trouble occurred between the companies for about fifteen years. During this time up to the 27th day of January, 1885, the Pullman Company paid to the Central Company, as rent under the contract, the sum of \$3,960,000, without any computation of interest. About or just prior to January, 1885, differences arose between the companies. The Pullman Company claimed the right to terminate the contract under the eighth clause thereof, or else to pay a much smaller rent. The merits of the controversy are not material.

The two companies not agreeing, and the Pullman Company refusing to pay the rent stipulated for in the lease, the Central Company brought successive actions to recover the instalments of rent accruing. In one of them the Pullman Company pleaded the illegality of the lease, as being ultra vires the charter of the Central Company. The plea prevailed in the trial court, and upon writ of error the judgment upholding this defense was, in March, 1891, sustained in this court. *Central Transportation Company v. Pullman's Car Company*, 139 U. S. 24.

The present suit was brought by the Pullman Company to enjoin the Central Company from bringing any further suits for rent, the Pullman Company offering to return such of the demised property as was still in existence and to make compensation for the balance as far as the court should find it ought to do so. The Central Company answered the bill, denying many of its material allegations including the allegation that the lease was illegal. Subsequently the Central Company was permitted to file a cross-bill, in which it claimed to avail itself of the tenders made in the complainant's bill with respect to the return of the property and compensation, and asked for an accounting of all profits; that the Pullman Company should be adjudged to be a trustee for the Central Company of all

contracts of transportation, whether original, new or renewals, held by the Pullman Company with railway companies with which there were contracts of transportation with the Central Company at the time of the making of the lease, and that defendant should in the future, from time to time, account for the sums which should be due by reason of future operations under the contracts.

The Pullman Company made a motion for leave to dismiss its bill, and filed demurrers to the cross-bill. Leave to dismiss its bill was denied and the demurrers were overruled with leave to present the questions on final hearing.

MR. JUSTICE PECKHAM, after stating the facts, delivered the opinion of the court.

The facts which were set up in the cross-bill closely affected one of the theories upon which the original bill was filed, viz., the invalidity of the lease. They were relevant to the matters in issue in the original suit, and in seeking affirmative relief the cross-complainant is but amplifying and making clearer the foundations for the intervention of equity which had been appealed to by the Pullman Company, and the continued intervention of which would greatly speed a final termination of all matters for litigation between the parties. The court below did not err in permitting the cross-bill to be filed.

This brings us to a discussion of the principles upon which a recovery in this case should be founded. The so called lease mentioned in this case has been already pronounced illegal and void by this court. 139 U. S. 24. The contract or lease was held to be unlawful and void because it was beyond the powers conferred upon the Central Company by the legislature, and because it involved an abandonment by that company of its duty to the public. It was added that there was strong ground also for holding that the contract between the parties was void because in unreasonable restraint of trade, and therefore contrary to public policy. [In making the lease the lessor was certainly as much in fault as the lessee.] It was argued on the part of the Central Company that even if the contract sued on were void, yet that having been fully performed on the part of the lessor and the benefits of it received by the lessee for the period covered by the declaration in that case, the defendant should be estopped from setting up the invalidity of the contract as a defence to the action to recover compensation for that period. But it was answered that this argument, though sustained by the decisions in some of the States, finds no support in the judgments of this court, and cases in this court were cited in which such recoveries were denied.

It is true that courts in different States have allowed a recovery in such cases, among the latest of which is the case of Bath Gas Light Co. v. Claffy, 151 N. Y. 24, where CHIEF JUDGE ANDREWS of the Court of Appeals examines the various cases, and that court concurred with him in permitting a recovery of rent upon a void

lease where the lessee had enjoyed the benefits of the possession of the property of the lessor during the time for which the recovery of rent was sought.

But in the case of this lease, now before the court, a recovery of the rent due thereunder was denied the lessor, although the lessee had enjoyed the possession of the property in accordance with the terms of the lease. It was said (page 60 of the report in 139 U. S.), "the courts, while refusing to maintain any action upon the unlawful contract, have always striven to do justice between the parties so far as could be done consistently with adherence to law, by permitting property or money parted with on the faith of the unlawful contract to be recovered back or compensation to be made for it. In such case, however, the action is not maintained upon the unlawful contract nor according to its terms, but on an implied contract of the defendant to return, or failing to do that, to make compensation for the property or money which it had no right to retain." To maintain such an action was not to affirm, but disaffirm, the unlawful contract." And the opinion of the court ended with the statement that, "Whether this plaintiff could maintain any action against this defendant, in the nature of a quantum meruit, or otherwise, independently of the contract, need not be considered, because it is not presented by this record and has not been argued. This action, according to the declaration and evidence, was brought and prosecuted for the single purpose of recovering sums which the defendant had agreed to pay by the unlawful contract, and which, for the reasons and upon the authorities above stated, the defendant was not liable for."

The principle is not new; but, on the contrary, it has been frequently announced, commencing in cases considerably over a hundred years old. It was said by Lord Mansfield, in *Holman v. Johnson*, 1 Cowper, 341, decided in 1775, that "the objection that a contract is immoral or illegal as between the plaintiff and defendant, sounds at all times very ill in the mouth of the defendant. It is not for his sake, however, that the objection is ever allowed; but it is founded in general principles of policy, which the defendant has the advantage of, contrary to the real justice, as between him and the plaintiff, by accident, if I may so say. The principle of public policy is this: *ex dolo malo non oritur actio*. No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act."

The cases upholding this doctrine are numerous and emphatic. Indeed, there is really no dispute concerning it, but the matter of controversy in this case is as to the extent to which the doctrine should be applied to the facts herein. Many of the cases are referred to and commented upon in the opinion delivered in the case in 139 U. S. 24, already cited. The right to a recovery of the property transferred under an illegal contract is founded upon the implied promise to return or make compensation for it. For illustra-

tions of the general doctrine as applied to particular facts we refer in the margin to a few of the multitude of cases upon the subject.

They are substantially unanimous in expressing the view that in no way and through no channels, directly or indirectly, will the courts allow an action to be maintained for the recovery of property delivered under an illegal contract where, in order to maintain such recovery, it is necessary to have recourse to that contract. The right of recovery must rest upon a disaffirmance of the contract, and it is permitted only because of the desire of courts to do justice as far as possible to the party who has made payment or delivered property under a void agreement, and which in justice he ought to recover. But courts will not in such endeavor permit any recovery which will weaken the rule founded upon the principles of public policy already noticed.

We may now examine the record herein and learn the grounds for the recovery which has been permitted, and determine therefrom whether the judgment in favor of the Central Company should be in all things affirmed, or if not, then how far the liability of the cross-defendant extends, and, if possible, what should be the amount of the judgment against it.

(The learned judge was of the opinion that the court below erred in the manner of ascertaining the value and *held* that the Central Company was entitled to recover only the value of the property transferred under the lease, with interest, and was not entitled to recover the value of contracts with railroad companies or patents, all of which had expired, or anything for the breaking up of its business.)

Nor can we accede to the view that the Pullman Company is liable for the earnings of the property which it realized by means of putting such property to the very use which the lease provided. It had the right while both parties acquiesced to so use the property.

There is no question of trustee in the case. *Root v. Railway Company*, 105 U. S. 189, 215.

The property was placed in its hands by the lessor and in accordance with the terms of the agreement. It was not then impressed with any trust according to any definition of that term known to us. Although the title did not pass and was not intended to pass, the lessee did nothing with the property other than was justified by the lease. His liability is based only upon an implied promise to return or make compensation therefor. This implication of a promise would not arise until one or the other party chose to terminate the lease, for the law implies such promise in order only that justice, so far as possible, may be done. So long as neither party takes any objection to the agreement, and both carry it out, there is no room for any differences, and no promise to return the property or make compensation is necessary, and none is therefore implied. The use of the property is lawful as between the parties, so long as the lease was not repudiated by either, and the rent compen-

sates for the use. After the repudiation the promise is then implied, and it is fulfilled by the payment of the value of the property at the time the promise is implied and interest thereon from that time.

As to the claim of the lessor that its business has been broken up, its contracts with railroads terminated and the corporation left in a condition of inability to again take up its former plans, and that all this should be regarded in the measure of the relief to which it should be entitled, the same considerations which we have already adverted to must be entertained. These are results of the illegality of the contract entered into between these parties, and its subsequent repudiation on that ground, and in regard to such illegality the Central Company is certainly as much in the wrong as the cross-defendant herein. The former knew the extent of its obligations under its charter as well as the latter did, and the illegal provisions of the lease were quite as much its doing as they were those of the cross-defendant. [To grant relief based upon these facts would be so clearly to grant relief to one of the parties to an illegal contract, based upon the contract itself or upon alleged damages arising out of its non-fulfilment, that nothing more need be said upon that branch of the subject. It is emphatically an application of the rule that in such a case the position of the defendant is the better. * * *

Although the Central Company may have been injured by the result of this lease, yet that is a misfortune which has overtaken it by reason of the rule of law which declares void a lease of such a nature, and while the company may not have incurred any moral guilt it has nevertheless violated the law by making an illegal contract and one which was against public policy, and it must take such consequences as result therefrom.

The judgment appealed from must be *reversed* and the case remitted to the Circuit Court for the Eastern District of Pennsylvania, with directions to enter a judgment for the Central Transportation Company in accordance with this opinion.

MR. JUSTICE HARLAN dissented.

MR. JUSTICE WHITE dissented on the ground that the judgment appealed from was for the correct amount and should not be reduced.²²

HARRIS v. INDEPENDENCE GAS CO.

1907. 76 Kansas 750, 92 Pac. 1123.

THE opinion of the court was delivered by

MASON, J.—Cornelius Carr and his wife executed to the Independence Gas Company an oil-and-gas lease; that is, an instrument

²² See also Greenville etc. Warehouse Co. v. Planters' etc. Warehouse Co. (1893) 70 Miss. 669.—Eds.

granting the right to explore a tract of land for oil or gas and to appropriate either if found. The company is a Kansas corporation and at the time of the execution of the lease the only purpose mentioned in its charter was "to dig or mine for natural gas and sell the same for heat and lighting purposes." Later an amendment was made adding thereto the mining and selling of oil. What are called the "gas rights" under the lease have been transferred to another gas company and no point is raised with regard to them. The Carrs, claiming that the lease so far as it related to oil was void because at the time it was executed the lessee had no authority to engage in the oil business, undertook to grant the oil privileges anew to C. C. Harris, who upon that ground brought a suit against the Independence Company to cancel all of its contract excepting that portion relating to gas, joining his grantors as coplaintiffs. The trial court sustained a demurrer to a petition setting out substantially these facts and this proceeding is brought to review that ruling.

The defendant maintains: (1) That it had the implied power to produce and market oil as an incident to the express power granted to it to produce and market gas; (2) that if it originally lacked such power the defect was supplied by the charter amendment; and (3) that even if it had no authority to enter into the contract the plaintiffs cannot take advantage of the fact. It will only be necessary to consider the questions involved in the third proposition.

Although the decisions relating to the doctrine of ultra vires are characterized by some confusion as well as by much conflict, they admit of classification into fairly well-defined groups and exhibit a development in the direction of restricting the scope of its operation. Those courts which accord it the most favorable treatment—allow it the largest field of action—proceed upon the conception that a corporation, being the creature of the state, possesses no power whatever beyond that granted in its charter, and cannot directly or indirectly acquire rights or incur liabilities under any contract not thereby authorized. They refuse under any circumstances to enforce or give effect to an authorized contract, as such, but where it has been acted upon will protect the parties against hardship and injustice by allowing whatever relief may be suited to the facts of the case; for instance, by permitting either party to recover money or property which has been parted with in the transaction, or to have compensation therefor. The cases illustrating this treatment of the matter are collected in volume 29 of the American and English Encyclopædia of Law, at page 54, note 2. The theory is consistent and logical, but its practical effect is so to circumscribe the power of the court as to make the relief furnished at times inadequate to the occasion.

In a larger number of jurisdictions, although the same conception of corporate capacity is adopted, its effect is greatly changed by the application of another principle. Here the courts concede

that a corporation has no power to make a contract except such as is conferred by its charter, expressly or by necessary implication. But they hold that as it must have some discretion in the manner of carrying out the purposes of its creation—some freedom of action—it is amenable to the same rules of conduct as a natural person, and may estop itself to question the validity of an agreement it has assumed to make, or may acquire the right to invoke a similar estoppel in its own behalf. Where this theory is accepted recovery may be had upon a contract which is in fact void, simply because its validity cannot be put in issue. The cases in point are gathered in volume 29 of the American and English Encyclopædia of Law, at page 57, note 1.

These cases have been criticised for the use they make of the word "estoppel" as descriptive of the principle upon which they are based. It is argued that as a corporation must know the terms of its own charter, and as one dealing with it is charged with like knowledge, neither party to an ultra vires contract can be misled in that respect, and therefore there must always be lacking an essential element of what could with technical accuracy be called estoppel. This, however, is a mere question of terminology. The requirement that one shall be consistent in conduct—shall not occupy contradictory positions—shall not retain the advantages of a transaction and reject its burdens—is often spoken of as a form of estoppel.

The term is convenient, and, if inaccurate, is not misleading. This rule of estoppel affords a good working hypothesis to accomplish just results. If it fails to accomplish all that might be desired in a practical way it is because it is not made sufficiently far-reaching. It is generally held to be inapplicable to purely executory contracts, one reason stated being that "where neither party has acted upon the contract, the only injustice caused by a refusal to enforce it is the loss to the parties of prospective profits, and this is too slight a consideration to weigh against the reasons of public policy for declaring it void and not enforceable." (29 A. & E. Encycl. of L. 49.)

It might seem reasonable that a system which attempts not only to protect a party to an ultra vires contract from actual loss, but, where equity requires it, to insure to him the actual fruits of his bargain, ought for the sake of completeness and symmetry to enable him to insist upon the performance even of a purely executory contract. It certainly seems against conscience that one who has entered into a contract in the expectation of deriving a profit from it may upon discovering the probability of a loss repudiate it and escape responsibility by raising the question of want of corporate capacity. Parties to a contract who deal with each other upon the assumption that one of them is a corporation are ordinarily precluded from questioning the validity of its organization.

"Although, as against the state, a corporation cannot be created by the mere agreement, admission, assent, or other act or omission of private persons, yet, as between themselves and for the pur-

poses of their own private litigations and contestations, they may, by their agreements, their admissions, or their conduct, estop themselves from denying the fact of the existence of the corporation; so that for the purpose of such private litigations the body claiming to be a corporation, and having a colorable existence as such becomes such to all intents and purposes as much as though it were a corporation de jure. . . . A leading branch of the doctrine is that whenever a private person enters into a contract with a body purporting to be a corporation, in which contract the body is described by the corporate name which it has assumed, such private person solemnly admits the existence of the corporation for the purposes of the suit brought to enforce the obligation, and in such an action will not be permitted to plead nul tiel corporation or otherwise to deny the corporate existence of plaintiff. . . . One theory of the rule is that by entering into a contract with the assumed corporation as such the contracting party admits its existence and will not thereafter be permitted to change front and deny it. . . . The rule of estoppel works both ways. A body which has held itself out as a corporation and which has incurred obligations in a corporate name and character is, when proceeded against by the obligee, estopped to deny the regularity of its organization or otherwise to deny the validity of its corporate existence." (10 Cyc. 244-246, 249.)

The question whether a corporation has power under its charter to engage in a particular business is so like the question whether a body has capacity to act as a corporation at all as to afford good ground for arguing that whatever circumstances work an estoppel to raise the one have the same effect with respect to the other. This is recognized in volume 10 of the *Cyclopædia of Law and Procedure*, at page 248, where it is said:

"A person contracting with an ostensible corporation to do an act which is not prohibited by law becomes estopped, in an action by the corporation to enforce the contract, either to deny the existence of the corporation or its power to enter into such a contract."

The cases cited in support of this text, however, arose upon executed contracts, and we do not discover that the principle has actually been applied in actions upon purely executory agreements, unless where the question sought to be raised was whether a body assuming to act as a corporation had a legal existence as such. Nevertheless, no good ground is apparent for a distinction in this regard. A large majority of the adjudications on the subject of ultra vires fall into one or the other of the two groups already referred to. The conception of corporate power upon which they depend has been styled that of "special capacities," in distinction from that of "general capacities." (See article by George Wharton Pepper on "Exercise of Corporate Power," 9 Harv. L. R. 255.) The conception designated by the latter term is in brief that while a corporation has no right to exceed the limits of its charter it has

the power to do so. The theory was elaborated in the opinion of Mr. Chief Justice Comstock in the celebrated case of *Bissell v. The Michigan Southern and Northern Indiana Railroad Companies*, 22 N. Y. 258, where it was said:

"Like natural persons, they [corporations] can overleap the legal and moral restraints imposed upon them; in other words, they are capable of doing wrong. . . . The distinction between power and right is no more to be lost sight of in respect to artificial than in respect to natural persons. . . . Why, it may be asked, does the law provide the remedy by quo warranto against corporations for usurpation and abuse of power? Is it not the very foundation of that proceeding that corporations can and do perform acts and usurp franchises beyond the rightful authority conferred by their charters? Most assuredly this is so. The sovereign power of the state interposes, alleges the excess or abuse, and on that ground demands from the courts a sentence of forfeiture." (Pages 264, 265.)

These expressions were merely those of the chief justice, for the case was decided upon other considerations, but the theory presented has since been adopted by the New York courts. (See *Vought v. Eastern Bldg. & Loan Assn.*, 172 N. Y. 508, 65 N. E. 496, 92 Am. St. Rep. 761.) This theory, logically followed out, would obviously make all corporate contracts, executory as well as executed, enforceable between the parties. It has not, however, met with any large acceptance, at least in the form stated. (See, however, 29 A. & E. Encycl. of L. 45, note 2.) But a recent tendency has been developed to reach substantially the same result by a somewhat different course of reasoning, resulting in a doctrine which is thus stated in volume 10 of the *Cyclopædia of Law and Procedure*, at page 1164:

"A most important doctrine connected with this subject, and one which rises above the mere principle of estoppel, is that whether a corporation has acted without authority conferred on it by the legislature or has acted in contravention to an act of the legislature cannot be set up collaterally by individuals who deal with it, or by third persons, but can be set up only by the state in a direct proceeding to forfeit its charter, to oust it of some particular franchise, or to subject it to punishment; or where the question is otherwise litigated between the state and the corporation."

The cases applying or discussing the doctrine are collected in notes to this text and to succeeding paragraphs in the same work. The principle referred to, if sound, is manifestly sufficient in itself to defeat the defence of ultra vires even when interposed against the enforcement of an executory contract; but it must be admitted that in practice it seems to have been applied only where the agreements had been at least partially performed. It seems often to have been invoked, however, in aid of the ordinary doctrine of estoppel, in cases where the contract upon one side or the other had already

been performed. The best and most complete expression of it is found in the decisions of the Wisconsin court. In *John V. Farwell Co. v. Wolf and others*, 96 Wis. 10, 70 N. W. 289, 71 N. W. 109, 37 L. R. A. 138, 65 Am. St. Rep. 22, it was said:

"Judge Thompson, in his valuable treatise on the Law of Corporations (volume 5), commenting on the subject (secs. 6033-6038), appears to deprecate the prevalence of the 'new doctrine', and to argue against its further extension, upon the ground that it practically destroys the effect of the doctrine of ultra vires, as applied to the unauthorized exercise of corporate power; but the learned author is manifestly in error in that respect. Such doctrine, notwithstanding the limitation which modern development has placed on the means by which it may be called into use, still exists and may and will continue to exist, adapted as fully as ever to restrain the abuse of corporate franchises and authority, and to punish such abuse whenever the state, in its sovereign capacity, sees fit to exercise it. That such doctrine cannot be resorted to as a weapon for attack and defense in the hands of mere private persons, and used as a ready means of embarrassing business operations by and with corporate bodies, which directly or indirectly touch and administer to human desires at every turn of the individual in modern life, while its effectiveness for all essential purposes of restraint and punishment is fully preserved, furnishes no cause for regret, but rather cause for gratification at the evidence of how certainly principles, by natural growth and development, adapt the law and its administration to the ever-changing needs of advancing civilization, so as best to promote justice and the common welfare. When a corporation offends against the law of its creation, such offense is against the sovereignty of the state; hence it is most proper that the state should apply the remedy and be charged with the sole responsibility in that regard, and such is the law by the trend of modern authorities, which we approve." (Page 16.)

And in *The Zinc Carbonate Co. v. The First National Bank of Shullsburg*, 103 Wis. 125, 79 N. W. 229, 74 Am. St. Rep. 845:

"This and other courts have so often held that a corporation cannot violate its charter for pecuniary gain and retain the benefits of its illegal conduct by putting up the shield of ultra vires, or a person set himself up as the champion of the state in a court of justice to either punish or defend a corporation by an appeal to such doctrine in order to enable him or it to obtain or retain an unconscionable advantage, that we may safely reject the idea that it was thought a contrary view ruled the issue of law in the case adversely to appellant. The doctrine of ultra vires is a most powerful weapon to keep private corporations within their legitimate spheres and to punish them for violations of their corporate charters, and it probably is not invoked too often; but to place that power in the hands of the corporation itself, or a private individual, to be used by it

or him as a means of obtaining or retaining something of value which belongs to another, would turn an instrument intended to effect justice between the state and corporations into one of fraud as between the latter and innocent parties. Such is the modern doctrine, evolved and settled in the progress of events, reaching from the time when private corporations were few and the doctrine of *ultra vires* invoked quite as freely as to them as to public corporations, to a time when substantially all restrictions to the formation of such private bodies were removed, and they were authorized and commenced to exist, great and small, everywhere, for the purpose of conducting almost every kind of legitimate business. If such a body transcend its powers it commits a wrong against the state, and ordinarily it is for the state only to call it to account for such violation." (Page 131.)

And in *Security Nat. Bank v. St. Croix Power Co.*, 117 Wis. 211, 94 N. W. 74:

"This court, by a series of decisions, has held that, when a corporation enters into business relations not authorized by its corporate grant of power, the doctrine of *ultra vires* cannot be used by it or by the person with whom it assumes to deal as a means of defeating the obligations assumed.

The state alone can take advantage of the abuse. . . . The fact that this court has adopted the principle that the question cannot be litigated by private parties, a principle with which we are entirely satisfied, relieves us from further consideration of the question." (Pages 217, 218.)

None of these cases arose upon an executory contract, and in *John V. Farwell Co. v. Wolf* and others, *supra*, that consideration was referred to, the decision being expressly limited to the question before the court. But in *Security Nat. Bank v. St. Croix Power Co.*, *supra*, although the contract involved was in fact executed, the principle was broadly stated without reference to that matter, as shown by the quotation made from the opinion.

The principle referred to is closely allied to, if indeed it is not substantially identical with, that which forbids the regularity or validity of the organization of a corporation to be inquired into except at the instance of the state. (10 Cyc. 256.) The reason for such rule is thus stated in *Pape v. Capitol Bank*, 20 Kan. 440, 27 Am. Rep. 183:

"This is not upon the ground of equitable estoppel, but upon grounds of public policy. If the state, which alone can grant the authority to incorporate, remains silent during an open and notorious assertion and exercise of corporate powers, an individual will not, unless there be some powerful equity on his side, be permitted to raise the inquiry. The law holds out no such encouragement to attempt to avoid the payment of contract debts." (Page 445.)

The question whether a corporation has a legal existence is a question whether it has capacity to act at all. This is essentially of

the same character as the question whether it has capacity to enter into a particular contract—in other words, whether it has a legal existence for that purpose. The state grants the corporation the right to do business under limitations expressed in language to which both agree. Whether the language of the charter shall be interpreted to authorize a given act is a matter between the parties to it. If the state is satisfied with the construction upon which the corporation acts no reason is apparent why it should be open to question by a stranger, much less by one who has recognized it as valid by contracting with the corporation upon that basis.

This court has already held that a contract made by a corporation without authority may be rendered enforceable by estoppel. (*Town Co. v. Morris*, 43 Kan. 282, 23 Pac. 569.) It was there said that the rule did not apply to executory contracts, but that question was not involved. In *Morisette v. Howard*, 62 Kan. 463, 63 Pac. 756, other Kansas cases to the same effect are collected. The court there refers to the matter of collateral attack, saying:

"Aside from these considerations, the transaction had been completed, the money had been paid, the property had changed hands; all having been done with the knowledge and consent of those in whom the ultimate authority rested, and from whom the board of directors derived its power, the transaction, however irregular, is not open to attack by anyone other than the state." (Page 467.)

The case of *Scott v. Bankers' Union*, 73 Kan. 575, 85 Pac. 604, turned merely upon a matter of constructive notice. The notes sued upon were not enforceable unless they were held by an innocent holder. As was said in the opinion: "The scheme of consolidation failed. These notes were not to be paid unless it succeeded." (Page 588.) The question was not whether a corporation could be held to the terms of a contract to which it had agreed, but whether the law would attach to its promise to pay money the peculiar qualities of commercial paper. What was decided was that the corporation had no power to issue negotiable notes; that the purchaser was charged with notice of that fact, and therefore took them subject to any defenses that could have been made against the original holder.

The case of *Bankers' Union v. Crawford*, 67 Kan. 449, 73 Pac. 79, 100 Am. St. Rep. 465, growing out of the same transaction, can be distinguished from the one at bar on several grounds. The attempt there was to hold one assessment-insurance company for the payment of a beneficiary certificate issued by another on the theory that there had been a consolidation of the two. The contract of consolidation was held to be void as beyond the powers of either company. The corporations there involved were not ordinary business concerns. They possessed no corporate stock. The contract relied upon, to which the plaintiff was not a party, was one incapable of performance, and against good morals as involving a diversion of trust funds.

Very much the same principle as that already discussed was ap-

plied in *The State v. Book Co.*, 69 Kan. 1, 76 Pac. 411, 1 L. R. A., n. s., 1041, in denying the right of a party to a contract to demand its cancellation because of the failure of the other party—a foreign corporation—to comply with the statute relating to such organizations. In the opinion it was said:

“From this survey of the statute it appears that the legislature intended it to be complete; that the regulation of foreign corporations, and not the penalizing of business transactions, is its purpose; that such regulation is made the concern of the state in its special capacity as visitor, and not of any individual as a mere party to a contract; that a party to a contract is allowed to interfere in but a single instance, and then only to the extent of abating a suit against him; and that specific penalties are chosen to meet certain contingencies. The conclusion obviously and naturally follows that the legislature intended the state to rely upon the common-law remedies for the enforcement of the statute where none other was expressed; that the courts have no authority to interpolate in the law provisions concerning which the legislature, with all the resources of the English language at its command, remained silent, or to annex penalties for a violation of the law which the legislature, with a great arsenal to choose from, failed to mention. Hence contracts made with a foreign corporation before it has obtained permission to do business in the state are not, for that reason, invalid or subject to cancellation. . . . It is utterly illogical to compromise in a matter of interpretation, to palter with the status of such contracts and attempt to distinguish between those which are executed and those which are unexecuted, or to say they may be voidable if they are not void, or withhold remedies for a time. Such contracts are valid or invalid, and if valid are not subject to cancellation, and are enforceable as other contracts are enforceable, except as the law has restricted the corporation in its right to maintain an action or recover a judgment.” (Pages 7, 18.)

As in that case, the whole question here presented is as to the real intention of the legislature. A section of the corporation act reads:

“No corporation created under the provisions of this act shall employ its stock, means, assets, or other property, directly or indirectly, for any other purpose whatever than to accomplish the legitimate objects of its creation.” (Gen. Stat. 1901, § 1285.)

Such provisions are regarded, however, as merely declaratory and do not affect the ordinary rule as to the enforceability of contracts.

“A provision in a general corporation law that no corporation created thereunder shall employ its assets for any other purpose than to accomplish the legitimate objects of its creation is merely declaratory of the common-law rule by which corporations are confined in their powers to the purposes for which they are created, and does not amount to such an express statutory prohibition of ultra vires loans and other transactions as to render them illegal in-

stead of ultra vires merely." (1 Clark & Marshall, Priv. Corp., § 225b.)

No Kansas statute declares that a contract made by a corporation in excess of its legitimate powers shall be void, or in terms permits the question of corporate capacity to be raised by one of the parties. Where it is held that no recovery can ever be had upon an ultra vires contract, as such, whatever relief is afforded is logically made to turn upon whether and how far the agreement has been acted upon. Where a recovery is sometimes permitted under the contract itself, upon the principle of estoppel, the question whether it has been carried out is likewise of manifest importance, there being a difference in degree at least between the attitude of one who has merely entered into an engagement in expectation of obtaining an advantage from it and that of one who has actually reaped its benefits in whole or in part. But the doctrine that only the state can challenge the validity of acts done under color of a corporate charter, if accepted, must necessarily protect an executory contract from collateral attack equally with one that has been executed. The court is convinced of the soundness of the view that in the absence of special circumstances affecting the matter neither party to even an executory contract should be allowed to defeat its enforcement by the plea of ultra vires. The doctrine is logical in theory, simple in application, and just in result. It of course does not apply to contracts which are immoral or which are illegal, as distinguished from merely unauthorized, or to those made by public corporations. Nor does it forbid interference by a stock-holder to protect his rights as such. Upon these considerations the judgment is *affirmed*.

Section 4.—Ultra Vires Torts.

BATHE v. DECATUR COUNTY AGRICULTURE SOCIETY.

1887. 73 Iowa 11, 34 N. W. 484.

ACTION to recover for alleged injury to plaintiff's mare by defendant's employees. Demurrer to petition sustained and plaintiff appeals.

ADAMS, Ch. J.—The petition shows that the defendant is a corporation, organized to further the interest of agriculture, to improve and encourage the breeding of fine stock, to hold expositions of agricultural products and stock, to hold and give annual fairs, and to do and perform everything necessary and incident thereto; that in the fall of 1885 the defendant held its annual fair at its fair grounds in Decatur county, near the town of Leon; that, for the purpose of increasing the attendance and the gate receipts, the officers of the defendant employed one Clark and one Wilson to con-

vey people in their own conveyances from the town of Leon to the fair grounds; that Clark and Wilson, while so engaged, ran their team negligently against the plaintiff's mare, and caused her death. The defendant demurred to the petition, upon the ground, among others, that it does not appear that the defendant had authority to employ Clark and Wilson, as alleged, and thereby assume responsibility for their conduct as employees.

The powers of a corporation are such as are expressly provided in the articles of incorporation, and such others as are reasonably incident to the exercise of such powers. The plaintiff contends that the employment of Clark and Wilson to convey people to the fair grounds was incident to the holding of a successful fair; as there would be no fair without attendance. This might be conceded, if attendance depended upon conveyances provided by the defendant, and it was so understood by the members of the society at the time they joined it. But there is nothing in the petition which shows this to be so. In the absence of any showing to the contrary, we may assume that the members of the society joined it with the understanding that all persons desiring to attend the fair would be able to procure conveyances in their own way, and without any provision therefor by the society. Furnishing conveyances is a distinct business, in which any one might engage, and the presumption would be that the supply would be equal to the demand. In our opinion, then, there is nothing in the articles of incorporation, either by express provision, or arising therefrom by implication, that authorized the officers of the society to employ Clark and Wilson. If this is so, the defendant never became responsible for their conduct, and the demurrer to the petition was rightly sustained.

*Affirmed.*¹

NIMS v. MOUNT HERMON BOY'S SCHOOL.

1893. 160 Mass. 177, 35 N. E. 776.

KNOWLTON, J.—The defendant is an educational corporation. The plaintiff seeks to recover damages for an injury received through the negligence of a ferryman in managing a boat on which he was a passenger, and which, as he alleges, the defendant was

¹Gunn v. Central Railroad (1885) 74 Ga. 509; Weckler v. First Nat. Bank (1875) 42 Md. 581; Gillett v. Missouri etc. R. Co. (1874) 55 Mo. 315 (cf. Alexander v. Relfe (1881) 74 Mo. 495); Poulton v. London etc. R. Co. (1867) L. R. 2 Q. B. Cas. 534, *Accord.* See ~~Central R. R. & Banking Co. v. Smith~~ (1884) 76 Ala. 572 (tort not within authority of agent at fault).

"To fix the liability of a corporation for the tortious act of one of its employees, done in obedience to the commands of its officers, the act must be connected with the transaction of the business for which the company was incorporated. If the directors should order an agent to take a person out of his house and beat him, the corporation could not be held for the

using at a public ferry in the business of carrying passengers for hire. At the request of the defendant, the presiding justice ruled that there was no evidence to warrant a finding for the plaintiff, and directed a verdict for the defendant. The defendant contends that the ruling should be sustained on one or both of two grounds. It says in the first place, that, if it maintained the ferry and hired and paid the ferryman, the business was ultra vires, and therefore it is not liable for negligence in the management of the boat. Secondly, it contends that there was no evidence to connect the corporation with the business of running the ferry-boat, or to show that the ferryman was its servant.

It is a general rule that corporations are liable for their torts as natural persons are. It is no defense to an action for a tort to show that the corporation is not authorized by its charter to do wrong. Recovery may be had against corporations for assault and battery, for libel and for malicious prosecution, as well as for torts resulting from negligent management of the corporate business. *Moore v. Fitchburg Railroad*, 4 Gray, 465. *Reed v. Home Savings Bank*, 130 Mass. 443. *Fogg v. Boston & Lowell Railroad*, 148 Mass. 513. *Philadelphia, Wilmington & Baltimore Railroad v. Quigley*, 21 How. 202, 209. *Merchant's Bank v. State Bank*, 10 Wall. 604. *National Bank v. Graham*, 100 U. S. 699. *Gruber v. Washington & Jamesville Railroad*, 92 N. C. 1. *Hussey v. Norfolk Southern Railroad*, 98 N. C. 34. If a corporation by its officers or agents unlawfully injures a person, whether intentionally or negligently, it would be most unjust to allow it to escape responsibility on the ground that its act is ultra vires. The only plausible ground on which the defendant in the present case can contend that it should be exempt from liability for the negligence of its servant in managing the ferry-boat is that the contract to carry the plaintiff was ultra vires, and therefore invalid, and that the duty for neglect of which the plaintiff sues arose out of the contract, and disappears with it when the contract appears to be void. The defendant may argue that the plaintiff cannot maintain an action for a breach of the contract to use proper care to carry him safely, and that he stands no better when he sues in tort for failure to do the duty which grew out of the contract.

In *Bissell v. Michigan Southern & Northern Indiana Railroad*, 22 N. Y. 258, the plaintiff founded his action on the negligence of the two defendants while jointly running cars on a railroad in a State to which the charter of neither of them extended, and it was con-

assault and battery; or if the directors of a banking company should purchase a steamboat, and engage in transporting passengers, the corporation would not be liable for the misfeasance or non-feasance of agents employed in that business. But if the directors of a corporation having power to hold lands, order an agent to enter on lands and take possession of them for the legitimate uses of the company, his entry, if unlawful, will be the trespass of the corporation." *Depue, J., in Brokaw v. New Jersey R. etc. Co.* (1867) 32 N. J. Law 328, at page 332.—Eds.

ceded that the defendants were acting *ultra vires*. The plaintiff recovered, Comstock, C. J., holding in an elaborate opinion that the corporations were liable under their contract, notwithstanding that the contract was *ultra vires*, and that if they could not be held under their contract they could not be held at all, inasmuch as the only negligence alleged was a failure to use the care which the contract called for. Selden, J., in an equally full and elaborate opinion, held that the contract for carriage was invalid, and that there could be no recovery under it, nor for negligence founded upon it; but it was his opinion that, if the contract were set aside, the defendants owed the plaintiff a duty founded on his relation to them as an occupant, with their permission, of a place in their car, and that the improper management of the car was a neglect of that duty for which the plaintiff could recover. Clerke, J., agreed with this view, and all but one of the other judges concurred in a decision for the plaintiff, without stating the ground on which they thought the decision should be placed. This case was followed in *Buffet v. Troy & Boston Railroad*, 40 N. Y. 168, in which it was held that a railroad corporation was liable for negligence of the driver of a stage-coach which it was running without a legal right to do a business of that kind; but the opinion does not show whether the decision is founded on the opinion of Comstock, C. J., given in the former case, or on that of Selden, J. Like decisions have been made under similar facts in *Central Railroad & Banking Co. v. Smith*, 76 Ala. 572; *New York, Lake Erie, & Western Railway v. Haring*, 18 Vroom, 137; and *Hutchinson v. Western & Atlantic Railroad*, 6 Heisk. 634.

The better doctrine seems to be that a contract made by a corporation in violation of its charter, or in excess of the powers granted to it either expressly or by implication, is invalid considered merely as a contract, and, so long as it is entirely executory, will not be enforced. It is not only a violation of a private trust, viewed in reference to the stockholders, but it is against the policy of the law, which intends that corporations deriving their powers solely from the Legislature shall not pass beyond the limits of the field of activity in which they are permitted by their charter to work. *Monument National Bank v. Globe Works*, 101 Mass. 57. *Attorney General v. Tudor Ice Co.*, 104 Mass. 239. *Davis v. Old Colonial Railroad*, 131 Mass. 258. *Thomas v. Railroad Co.*, 101 U. S. 71. *Leslie v. Lorillard*, 110 N. Y. 519. *Linkauf v. Lombard*, 137 N. Y. 417. *East Anglian Railways v. Eastern Counties Railway*, 11 C. B. 775, 803. On the other hand, courts have frequently held that, while such contracts considered merely as contracts are invalid, they involve no such element of moral or legal wrong as to forbid their enforcement if there has been such action under them as to work injustice if they are set aside. Courts have been astute to discover something in the nature of an equitable estoppel against one who, after entering into such a contract, and inducing a change of condition by another party, attempts to avoid the contract by a plea of *ultra vires*. It is said that

such a plea will not avail when to allow it would work injustice and accomplish legal wrong. *Leslie v. Lorillard*, 110 N. Y. 519. *Linkauf v. Lombard*, 137 N. Y. 417, 423. Many cases might be supposed in which it would be most unjust to hold that one who had received the benefits of such a contract might retain them and leave the other party without remedy, as he might do in a supposable case, where another had put himself at a disadvantage on the faith of a contract with him to commit a crime. Whether in this Commonwealth a contract entered into by a corporation ultra vires, and partly performed, will ever be enforced on equitable grounds, we need not now decide. See *McCluer v. Manchester & Lawrence Railroad*, 13 Gray, 124; *National Pemberton Bank v. Porter*, 125 Mass. 333; *Attleborough National Bank v. Rogers*, 125 Mass. 339; *Atlas National Bank v. Savery*, 127 Mass. 75, 77; *Slater Woollen Co. v. Lamb*, 143 Mass. 420; *Prescott National Bank v. Butler*, 157 Mass. 548; *National Bank v. Mathews*, 98 U. S. 621; *National Bank v. Whitney*, 103 U. S. 99; *Parish v. Wheeler*, 22 N. Y. 494; *Oil Creek & Allegheny River Railroad v. Pennsylvania Transportation Co.*, 83 Penn. St. 160; *Bradley v. Ballard*, 55 Ill. 413. In the present case we think it makes no difference that the defendant was not a manufacturing or trading corporation, but was chartered for educational purposes only. It could acquire and hold property, make contracts, and do anything else incidental to the maintenance of the school. Doubtless some of its officers or agents thought it would be an advantage to its students and managers to have a public ferry at the place where the plaintiff was injured. Its maintenance of such a ferry was ultra vires, but its acts in that respect were not different in kind from the ordinary acts of corporations in excess of the powers given them by their charter. We are of opinion, therefore, that if the defendant while running the ferry-boat accepted the plaintiff as a passenger to be transported for hire, and undertook to carry him across the river, he was in the boat as a licensee, it owed him the duty to use proper care to carry him safely, and, whether an action could be maintained for a breach of the contract or not, it is liable to the plaintiff in an action of tort for neglect of that duty.

The other question in the case is whether there was evidence that the corporation operated the ferry. Under its by-laws the management of the corporation is vested in a board of trustees. It does not appear that any vote was ever taken in regard to the ferry, and it was not shown that any officer of the corporation took out the license which was granted to the defendant by the county commissioners, under Pub. Sts. c. 55, § 1, to keep the ferry, but the records of the county commissioners show that such a license was granted, and that a bond with sureties was given to the county of Franklin, with the condition properly to perform the duty of a ferryman, executed in behalf of the defendant by one who was designated as superintendent, and witnessed by the defendant's cashier and paymaster. It further appeared that the title to the property used at the ferry was

taken by Ambert G. Moody, one of the trustees of the defendant, who was then a student in Amherst College, and that he paid for it only a nominal sum above the mortgage existing upon it, and that he and the defendant's superintendent, who had charge of its farm, employed one Deane to operate the ferry, who was paid by the month, and who turned over the balance of the receipts of the ferry above his wages to the defendant's cashier and paymaster. For the month of April Deane was paid for his services by the defendant's paymaster out of the defendant's funds. In June, 1890, a new ferry-boat was constructed under an arrangement with Ambert G. Moody and Dwight L. Moody, both of whom were trustees of the corporation, and was paid for by the paymaster out of the funds of the corporation. For six months, and until there was a change in the management of the ferry, the defendant's cashier and paymaster sent to the treasurer, who lived in New York, monthly accounts, showing monthly receipts and expenses on account of the ferry. Accompanying the first of these accounts was a statement that the school was running the ferry and paying the bills. The treasurer was himself a trustee of the corporation. He subsequently rendered his official report to the corporation, which was audited by another of the trustees, who did not examine the items in person, but caused the examination to be made by a man in his employment. This report was accepted by the trustees and placed on file. The items of receipts and expenditures were entered on the books of the treasurer in an account under the title "ferry". The treasurer's report was not put in evidence, and was not produced, although the defendant was notified to produce it.

There is no evidence of original authority from the defendant to anybody to operate the ferry on its account, but the evidence is plenary that persons connected with the management of its business assumed so to operate it. The important question is whether there was evidence that the corporation ratified the acts of these persons. We are of opinion that there was evidence from which the jury might have found such ratification. It is not necessary that the ratification should be by a formal vote. It is enough if the corporation, acting through its managing officers, knowing that the business had been done by those who assumed to act as its agents in doing it, and that the income of the business had been received and the expenses of it paid by its treasurer in his official capacity, and that the balance of the receipts above the expenditures was in its treasury, adopted the action of its treasurer, and elected to keep the money. It was a fair inference of fact, especially when the corporation failed to produce the treasurer's report after notice to produce it, that the report contained a true statement of the accounts which related to the ferry, and that it was accepted with full knowledge on the part of the trustees of what it contained. Whether there was a ratification by the corporation was a question of fact for the jury on all the evidence.

If there was such a ratification, it carried with it the consequences

which would have followed an original authority. In *Dempsey v. Chambers*, 154 Mass. 330, it was held, after much consideration, that ratification of an unauthorized act would make the principal liable in an action of tort for an injury resulting from negligence of the agent in doing the act.

We are of opinion that the case should have been submitted to the jury.

Exceptions sustained.

HANNON v. SIEGEL-COOPER CO.

1901. 167 N. Y. 244, 60 N. E. 597.

APPEAL from a judgment of the Appellate Division of the Supreme Court in the second judicial department, entered June 15, 1900, affirming a judgment in favor of plaintiff entered upon a verdict and an order denying a motion for a new trial.

The nature of the action and the facts, so far as material, are stated in the opinion.

CULLEN, J.—The complaint charged that the defendant, a corporation, conducting a department store in the city of New York, represented and advertised itself as carrying on the practice of dentistry in one of its departments; that the plaintiff employed the defendant to render the necessary professional labor in the treatment of her teeth and paid therefor; that the defendant's servant performed said work so carelessly, negligently and unskillfully that plaintiff's jaws and gums were injured, for which malpractice she claimed damages. The answer in substance was a general denial. Plaintiff had a verdict at the Trial Term and the judgment on that verdict has been unanimously affirmed by the Appellate Division.

The Public Health Law by section 164 makes it a misdemeanor for any person to practise or to hold himself out to the public as practising dentistry in any county in this state without being licensed to practise as such and registered in the office of the clerk of the county, and it would seem that the action of the defendant in assuming to carry on the business of dentistry was illegal and ultra vires. But though it was beyond the corporate powers of the defendant to engage in the business this does not relieve it from the torts of its servants committed therein (*Bissell v. Mich. Southern R. R. Co.*, 22 N. Y. 258) and the unanimous affirmance of the Appellate Division is conclusive to the effect that it either practised dentistry or held itself out as practising dentistry. The only question cognizable by us arises upon the appellant's exception to the following charge of the trial court: "If the defendants in this case made representations to the plaintiff, on which she relied, that they were conducting a dentist business in their store, and if she, because of those representations, hired the workman in the store of the defendants, with no

knowledge that the business was conducted by Mr. Hayes individually, you may find the defendants responsible for the acts of the dentist who treated the plaintiff, even though Mr. Hayes, as a matter of fact, was the real owner of that department of the defendant's store." The appellants' counsel does not deny the general doctrine that a person is estopped from denying his liability for the conduct of one whom he holds out as his agent against persons who contract with him on the faith of the apparent agency, but he insists that the doctrine does not apply to the present case, because the action is brought in tort and not on contract. It may very well be that where the duty, the violation of which constitutes the tort sued for, springs from no contract with, nor relation to, the principal, a party would not be estopped from denying that the wrongdoer was his agent, even though he had held him out as such. In such a case the representation of the principal would be no factor in producing the injury complained of. But whenever the tort consists of a violation of a duty which springs from the contract between the parties, the ostensible principal should be liable to the same extent in an action *ex delicto* as in one *ex contractu*. It is urged that the representation that the operating dentists were the defendant's servants did not mislead the plaintiff to her injury and, therefore, should not estop the defendant from asserting the truth. There is no force in this claim. If A contracts with the ostensible agent of B for the purchase of goods, he relies not only on the business reputation of B, as to the goods he manufactures or sells, but on the pecuniary responsibility of B to answer for any default in carrying out the contract. [So here the plaintiff had a right to rely not only on the presumption that the defendant would employ a skillful dentist as its servant, but also on the fact that if that servant, whether skillful or not, was guilty of any malpractice, she had a responsible party to answer therefor in damages.]

The judgment appealed from should be affirmed, with costs.

O'BRIEN, BARTLETT, MARTIN, VANN and LONDON, JJ., concur; PARKER, Ch. J., takes no part.

*Judgment affirmed.*²

² In the following cases, corporations were held liable for torts committed in the course of an *ultra vires* undertaking. *South etc. R. Co. v. Chappell* (1878) 61 Ala. 527; *New York, etc. R. Co. v. Haring* (1885) 47 N. J. Law 137; *Bissell v. Michigan etc. R. Co.* (1860) 22 N. Y. 258 (per Selden, J.); *Fishkill Savings Institution v. National Bank* (1880) 80 N. Y. 162; *Gruber v. Washington etc. R. Co.* (1885) 92 N. Car. 1; *Hutchinson v. Western etc. R. Co.* (1871) 6 Heisk. (Tenn.) 634; *Zinc Carbonate Co. v. First Nat. Bank* (1899) 103 Wis. 125, 79 N. W. 229; *National Bank v. Graham* (1879) 100 U. S. 699, 25 L. ed. 750 ("Corporations are liable for every wrong they commit, and in such cases the doctrine of *ultra vires* has no application."); *Chesapeake & Ohio R. Co. v. Howard* (1900) 178 U. S. 153, 44 L. ed. 1015, 20 Sup. Ct. 880.—Eds.

CHAPTER VI.

SUBSCRIBERS. SUBSCRIPTIONS TO STOCK.

Section 1.—Subscriber as Distinguished from Stockholder.

MT. STERLING COALROAD CO. v. LITTLE.

1879. 14 Bush (Ky.) 429.

JUDGE ELLIOTT delivered the opinion of the court.

This action was brought by appellant on the following writing :

"The undersigned propose to subscribe for the number of shares of \$50 each to the capital stock of the Mt. Sterling Coalroad Company, when the charter shall have been obtained and the company organized, provided that the company receives our subscription, payable as follows, viz., ten per cent. on or before February 1, 1874, and by calls not exceeding ten per cent. per month thereafter until paid. Wm. Little, ten shares."

By the plaintiff's petition this instrument signed by appellee is treated as a subscription of ten shares of stock in the coalroad company, and on allegation of non-payment judgment is sought for the amount of the ten shares, which, it is alleged, appellee subscribed.

There is no allegation that the appellant ever delivered or tendered to the appellee the ten shares of stock, but instead thereof it is alleged that it received the appellee's subscription.

The writing sued on does not amount to a subscription of stock to appellant's company. It is only, as its language imports, a proposition to subscribe ten shares of \$50 each after the company shall have obtained its charter and perfected its organization, provided appellee should be permitted to pay ten per cent. of his subscribed stock on the 1st of February, 1874, and the balance in calls of not exceeding ten per cent per month.

We regard the reasoning of the court in the case of Thrasher v. Pike County Railroad Company, 25 Illinois Reports, page 393, as conclusive of this case. In that case the agents of the company, before its organization, agreed and promised to receive Thrasher's subscription of \$3,000 to the capital stock of the company, and it is then averred that Thrasher, "in consideration of this promise, undertook and promised the plaintiff that he would subscribe to the stock of this company the sum of \$3,000 when the books should be open

for subscriptions, and that this promise was, by writing, signed by the defendant, and by him delivered to the plaintiff."

The plaintiff then averred that the subscription-books were opened and subscriptions solicited, of which the defendant had notice; and it further averred that the defendant's subscription was due when the company's books were opened, which was before the commencement of the suit, and that the defendant, after request, had refused to pay any part of his subscription of \$3,000.

In that case, as in this, the action treated the writing sued on as a subscription, but the court, in that case, said that "this we do not think is a fair view of the defendant's liability upon his promise, if one was made to the plaintiff. His undertaking is to subscribe a certain amount of stock when the subscription books should be opened. This promise does not make him a stockholder, and as such liable to calls.

"The company has parted with no stock to him, and can only claim as damages the actual loss sustained by it by his failure or refusal to subscribe when he was notified the books were opened for such purpose.

"The company has the stock which the defendant promised to take but did not take. His promise is like any other agreement to purchase any specific article of property. If the property contracted for be retained by the vendor, and there is no delivery to the purchaser, or offer to deliver, the damages must not be measured by the value of the property, for it would not be just in such cases that the vendor should retain the property and recover also the value of it from the promisor. Some damage might result from the loss of a bargain, and to such the vendor would be entitled if the extent could be established."

In that case the court held that, in a suit to recover for the defendant's failure to subscribe, the measure of damages would likely have been the difference between the market and par value of the stock. The same doctrine is held in Pennsylvania. (See 21 Pa. 220.)

This doctrine accords with our views of this contract. The appellant has parted with nothing and the appellee has received nothing, and the appellant's petition is insufficient for the recovery of damages for the breach of appellee's contract to subscribe ten shares of stock in its company.

As this was not a suit for damages for a breach of appellee's contract to subscribe stock in appellant's company in pursuance of his written proposition, the judgment of the court sustaining a demurrer to the appellant's petition must be sustained, and as the appellant refused to plead further, the court properly dismissed the suit.

Wherefore the judgment is *affirmed*.¹

¹ Thrasher v. Pike County R. Co. (1861) 25 Ill. 393; Quick v. Lemon (1883) 105 Ill. 578, esp. 585; Strasburg R. Co. v. Echternacht (1853) 21 Pa. St. 220, 60 Am. Dec. 49, *Accord*. Cf. In re Hooley (1899) 2 O. B. 579.

But see *Butlock v. Falmouth etc. Turnpike Co.* (1887) 85 Ky. 184, 3 S. W.

BURR v. WILCOX.

1860. 22 N. Y. 551.

APPEAL from the Superior Court of the city of New York. Action to recover from the defendant the sum of \$1,000 and interest from June 23, 1858, when the suit was commenced, on account of a judgment for \$1,756.98 upon a debt contracted by the Hudson River Stone Dressing Company on the 19th of January, 1854. The complaint alleges that Elisha C. Wilcox, the defendant's testator, was a stockholder in said company to the amount of \$1,000, and as such was, in his lifetime, liable for said debt to the amount of his stock, under the personal liability provisions of the general law (ch. 40 of 1848) for the incorporation of manufacturing companies.

Upon the trial, these facts were admitted: A certificate of ten shares of the capital stock, dated February 6, 1854, was issued to Wilcox. This stock was apportioned to one Samuel H. Jordan for Wilcox, on the 15th of April, 1853, pursuant to a subscription for capital stock, originally made by Jordan for Wilcox, and at his request—the amount subscribed for to be paid in ten equal monthly installments. Wilcox paid all the installments—the first payment being on the 3rd of May, 1853.

Wilcox was not one of the signers of the articles of association, and derived such interest as he had in its stock from the facts before stated. A by-law of the company, which was in force during its whole existence, declared that the stock of the corporation was transferable only on its transfer-book, by the holder thereof or his attorney, on the surrender of his certificate. No stock transfer whatever to Wilcox was contained in the transfer-book of the company, and no shares of the company's stock had ever been transferred to the defendant's testator, or to any other person or persons for him or his use, on the transfer-books.

129 (*per* Bennett, J.): "Where a company is authorized to issue its capital stock, and put it upon the market for sale; and a person wishing to purchase the stock, as stock, merely as a judicious investment, agrees with the company to purchase so much of the stock at an agreed price; and the company, without having delivered the stock or tendered it to the purchaser, sues for the recovery of the agreed price,—then the rule is that the company cannot maintain such an action, because the company still holds the property, and the law will not permit it to withhold the property from the purchaser, and recover the agreed price of it.) In such a case, the company's remedy would be confined to an action for the recovery of such damages as it might have sustained, such as the loss of a bargain by reason of the purchaser's failure to comply with his contract. This rule was correctly stated in the case of *Mt. Sterling &c. Road Company v. Little*, 14 Bush (Ky.) 429; but the rule, by inadvertence, was incorrectly applied to the state of facts before the court. * * * To the extent that the opinion in that case was made to apply to the facts of it, it is overruled."

As to the distinction between agreements to subscribe and subscriptions, see also *Twin Creek etc. Road Co. v. Lancaster* (1881) 79 Ky. 552; *Van Schaick v. Mackin* (1908) 129 App. Div. (N. Y.) 335, 113 N. Y. S. 408.—Eds.

The plaintiff had a verdict, subject to the opinion of the court, which, at general term, rendered judgment in his favor. The defendant appealed to this court. The cause was submitted on printed arguments.

CLERKE, J.—

* * * The appellant's counsel seems to insist that a transfer of stock in a transfer book is necessary to constitute a person a stockholder. After the original issue of stock, perhaps, any subsequent holders, in order to be made liable, should have the stock transferred to them on the books, or their names as stockholders should appear in the index book, or in the register of stockholders. But, in the present case, Wilcox was an original subscriber, through his agent Jordan; and, of course, no transfer, as from an old to a new stockholder, was requisite. The stock was issued, not transferred, to him.

The judgment of the Superior Court of New York should be affirmed.

SELDEN, J.—The statute upon which this action is founded (Sess. Laws of 1848, ch. 40, § 10), makes the "stockholders of every company" incorporated under the act of which that section is a part, liable to the creditors of the company to an amount equal to the amount of stock which they hold. It is contended that the term stockholders, as here used, includes such persons only as hold the legal title to the stock of the company, and that the defendant's testator was never such a stockholder in the Hudson River Stone-Dressing Company, for two reasons: 1. Because he never obtained any assignment or transfer from Samuel H. Jordan, in whose name the original subscription was made; and, 2. Because no person could be a stockholder until stock was transferred to him upon the transfer book, in the manner prescribed by the by-laws of the company.

The first of these objections is sufficiently answered by the admitted facts, that the subscription was made by Jordan for the benefit of Wilcox; that the latter paid the installments; and that the company recognized his ownership of the stock, and issued the certificate to him. The fact that Jordan used his own name in subscribing gave him no right to insist that the company should recognize him as the owner of the stock, after it was made to appear that he was a mere agent for Wilcox, who alone had any interest in the stock. * * *

The second reason given why Wilcox never became a stockholder, viz., that there was no transfer to him upon the transfer book, is founded upon a misapprehension of the effect of the statutory provision that the stock should be transferable in such manner as should be prescribed by the by-laws of the company, and of the by-law adopted in pursuance thereof. This provision has reference solely to the transfer of stock from one stockholder to another, and not at all to the original issue of the certificates of stock by the company to its subscribers. That this was so understood by the company, is shown by the by-law itself, which provides that the stock should be transferred only upon the transfer book and on surrender of

the certificate, &c. A previous issue of the certificates of stock is, therefore, assumed.

There can, I think, be no doubt that this is the true construction of the statute. The issuing of the original certificates is in no sense a transfer of stock. The interest of the parties to whom they are issued is the same before as after such issue. The certificate is simply a written acknowledgment by the company of the interest of the subscribers in its property and franchises. It transfers nothing from the company to the subscriber, but simply affords to the latter evidence of his right. The by-law, therefore, could have no application to the act of the company in issuing its certificates to the various subscribers for their respective shares.

It follows conclusively, from these views, that Wilcox was a legitimate stockholder of the company, and held the legal title to the shares of stock mentioned in the certificate issued in his name. It is unnecessary, therefore, to consider the question whether the mere equitable owners of stock, the legal title to which is held by others, are liable under the statute in question.

But it is further contended that, if Wilcox was ever a stockholder, he did not become such until after this debt was contracted, and, hence, that the statute liability upon which this action is founded does not attach. The first apportionment of the stock was on the 15th of April, 1853. At that time ten shares were assigned or apportioned to "Jordan for Wilcox," as appears by the records of the company; but the certificate issued to Wilcox for these shares bears date the 6th day of February, 1854, and the entry in the book containing the alphabetical list of stockholders is as follows: "Feb. 6th, 1854, E. C. Wilcox, ten shares." The plaintiff's debt was contracted on the 19th of January, 1854. If, then, as is claimed, the testator, Elisha C. Wilcox, never became a stockholder until the certificate was issued and his name entered in the index book, it would be necessary to determine whether he could be made liable under the statute for a debt previously contracted. If, on the other hand, he became a "stockholder" before or at the time of the apportionment, no such question could arise.

The word stock has various significations; but, as applied to a joint stock association or corporation, it means the property and franchises of the corporation. It is sometimes used to designate the certificate, or scrip, issued to the stockholders; but this is an inappropriate use of the word. The scrip is not the stock. The moment a corporation has either franchises or property of any kind it has stock; and the distributive share of its members respectively, in this stock, will depend upon the terms of its charter or articles of association. Whether subscribers to the stock of this particular corporation acquired any legal interest in its property prior to the apportionment upon the 15th of April, 1853, could only be determined by an examination of its certificate of incorporation and the history of its formation. But at that time, if not before, every person to whom shares were then

assigned by the trustees acquired a proprietary interest in the stock of the company, if it then had property or valuable rights, and if not, then as soon as any was obtained, to the extent of the share or shares so assigned. No further act on the part of the company was necessary, in order to invest them with this interest.

But it seems to be supposed by the counsel for the defendant that, because section 25 of the act in question makes it the duty of the company to keep a book containing a list of the names of the stockholders alphabetically arranged, therefore no one could become a stockholder within the meaning of the law until his name was entered in that book. This is, manifestly, erroneous. The statute could not have that effect, unless it was made an absolute condition that, to constitute a stockholder, the name must be so entered. It contains, however, nothing of this kind. It simply imposes a duty upon the company, the penalty for the neglect of which would be a forfeiture to the public of the corporate franchise. It certainly was not intended to enable the company to exempt the actual owners of its stock from the liabilities imposed by the act by omitting to enter their names in the index book, which would be the effect of the construction insisted upon by the defendant's counsel. The testator, Elisha C. Wilcox, became, without doubt, a stockholder within the meaning of the act, from the time when his interest in the property or stock of the company accrued, which, in any view which can be taken of the facts, was long before the debt in controversy was contracted.

This disposes of the case, with the exception of the point made upon the allowance of interest. The language of the statute is, that the stockholders "shall be severally individually liable to the creditors of the company in which they are stockholders to an amount equal to the amount of stock held by them respectively," &c. This liability cannot, I think, be said to attach upon any particular stockholder until a suit is commenced against him to enforce it. The creditor has a right to select among the stockholders the individual against whom he will proceed; and until he has made this selection, no particular stockholder is liable, and hence no interest can be allowed for any previous time. But, from the time of the commencement of a suit for a debt exceeding the amount of the principal of the defendant's stock, I see no reason why interest should not be allowed. It has then become a fixed liability for a specific amount, and ought, upon general principles, to carry interest.

The judgment of the Superior Court should be affirmed.

All the judges concurring.

*Judgment affirmed.*²

² See also *California Southern Hotel Co. v. Callender* (1892) 94 Cal. 120, 29 Pac. 859; *Fulgam v. Macon etc. R. Co.* (1872) 44 Ga. 597; *Corwith v. Culver* (1873) 69 Ill. 502; *Wemple v. St. Louis etc. R. Co.* (1887) 120 Ill. 196, 11 N. E. 906 (distinguishing contract of subscription to capital stock of a corporation from a contract for the purchase of shares); *Wuller v. Chuse Grocery Co.* (1909) 241 Ill. 398, 89 N. E. 796; *Butler Univ. v. Scoonover*

WAUKON & MISSISSIPPI R. CO. v. DWYER.

1878. 49 Iowa 121.

ACTION to recover upon a subscription to the stock of the plaintiff company. The contract of subscription is in the following words:

"We, the undersigned, do hereby agree to take stock in the Waukon & Mississippi Railroad to the amount of the number of shares set opposite to our names, respectively, subject always to the by-laws, rules, and articles of incorporation of the Waukon & Mississippi Railroad.

"Martin Dwyer, 1 share."

The petition avers that the defendant signed and delivered to the plaintiff an agreement in writing, of which the foregoing is a copy. It also sets out one of the articles of incorporation, which is as follows:

"Article IV. Said stock shall be divided into shares of one hundred dollars each, ten per cent of which shall be paid on the 15th

(1887) 114 Ind. 381, 16 N. E. 642; *Smith v. Gower* (1865) 63 Ky. 17; *Barron v. Burrill* (1893) 86 Maine 66, 25 Atl. 939; *Marson v. Deither* (1892) 49 Minn. 423, 52 N. W. 38; *Hawley v. Upton* (1880) 102 U. S. 314, 26 L. ed. 179; *South Dakota v. North Carolina* (1903) 192 U. S. 286, 309, 24 Sup. Ct. 269; *Blyth's Case* (1876) L. R. 4 Ch. Div. 140.

St. Paul & C. R. Co. v. Robbins (1877) 23 Minn. 439; *Swazey v. Choate Mfg. Co.* (1868) 48 N. H. 200 (*semble*), *Contra*. See *Charlotte etc. R. Co. v. Blakely* (1848) 3 Strobr. (S. Car.) 245; *In Re Florence Land & C. Co.* (1885) L. R. 29 Ch. Div. 421.

Parties may contract that the stock shall not be paid for until the certificate therefor has been issued and delivered or tendered. Thus, *cf. Summers v. Sleeth* (1874) 45 Ind. 598, with *Miller v. Wildcat Gravel Road Co.* (1875) 52 Ind. 51.

WHEELER v. MILLAR (1882) 90 N. Y. 353. Action against defendant as stockholder to charge him with indebtedness of corporation. It was proved that defendant was one of the original incorporators and that he subscribed for fifty shares of stock, but did not pay for them; that he was trustee and secretary of the corporation and actively engaged in its management. *Held*, defendant liable. Neither the issue of a certificate nor the payment is necessary. *Finch, J.*, said (pp. 358-9): "A share of stock like other property may be sold on credit. The title may pass, the right become vested, if such be the intention and contract of the parties, although payment is deferred and the usual written evidence of title is absent. Whatever may be said of the case where no fact is present as the foundation of an inference that title has passed, except the bare fact of a subscription, it is entirely reasonable that where, in addition, the corporation has explicitly recognized the alleged stockholder as such, and the latter has acted in that capacity, such fact should be deemed sufficient to justify a conclusion of ownership, and make the subscriber a stockholder. Certainly the rule has been carried even further than this (*Spear v. Crawford*, 14 Wend. 20; *Burr v. Wilcox*, 22 N. Y. 551); but whether correctly or not it is unnecessary at present to consider."

See also *Beales v. Buffalo & C. Construction Co.* (1900) 49 App. Div. (N. Y.) 589, 63 N. Y. Supp. 635 (statutory requirement that stock shall be represented by certificate does not change the rule).

PACIFIC NATIONAL BANK v. EATON (1890) 141 U. S. 227, 11 Sup. Ct. 984; *held* that subscription to stock in a national bank, payment in full on the sub-

day of the month after five hundred shares have been subscribed, and ten per cent shall be paid on the 15th day of each succeeding month thereafter until the whole is paid, as the expenditures require."

The petition further avers that five hundred shares were subscribed on the 1st day of April, 1875; that the plaintiff has completed its road; that the expenditures require full payment of the stock; and that defendant was duly notified on the 15th of each month that payment was required of the different installments as provided; but that the defendant had refused to pay the same.

To the petition the defendant filed a demurrer, which is as follows:

"1. That the facts stated in the petition do not entitle the plaintiff to the relief demanded, and alleges the following, to wit: Said petition shows this action to be upon a written contract, and does not show that said contract was ever made to or with the plaintiff, or indorsed to plaintiff. It does not show any right or necessity in plaintiff to sue upon the said contract, or that the plaintiff is the real party in interest in this suit. It does not allege that the defendant ever promised to pay plaintiff or any person money in any sum whatever, nor that any sum is due from the defendant to plaintiff on the contract set out in the plaintiff's petition.

"Said petition does not show to and with whom the said contract was made, nor that the plaintiff or person to and with whom it was made has performed all the conditions of said contract on his part. It does not show that the defendant is a stockholder in the Waukon & Mississippi Railroad Company as a corporation, nor that he is in any way liable to said plaintiff for assessments of shares of plaintiff's capital stock, nor that he ever subscribed to the articles of incorporation or by-laws of said company, or ever accepted stock, or is entitled to any of the stock of said corporation; nor that any of said

scription and entry of the subscriber's name in the stock register of the bank as a stockholder constituted the subscriber a shareholder though no certificate was ever taken out. *Per* Bradley, J.: "The only question to be considered, therefore, is whether the fact that the defendant in error did not call for and take her certificate of stock made any difference as to her status as a stockholder. We cannot see how it could make the slightest difference. Her actually going or sending to the bank and electing to take her share of the new stock, and paying for it in cash, and receiving a receipt for the same in the form above set forth, are acts which are fully equivalent to a subscription to the stock in writing, and the payment of the money therefor. She then became a stockholder. She was properly entered as such on the stock-book of the company, and her certificate of stock was made out ready for her when she should call for it. It was her certificate. She could have compelled its delivery had it been refused. Whether she called for it or not was a matter of no consequence whatever in reference to her rights and duties. * * * Millions of dollars of capital stock are held without any certificate, or, if certificates are made out, without their ever being delivered. A certificate is authentic evidence of title to stock; but it is not the stock itself, nor is it necessary to the existence of the stock. It certifies to a fact which exists independently of itself."—Eds.

stock was ever issued, offered or tendered to defendant by plaintiff, and the price thereof demanded of defendant.

"It does not show any promise by defendant to plaintiff as a corporation to pay to plaintiff the sum of one hundred dollars, nor any other sum, as a subscription to and for one share of the capital stock of said company, or as a contribution; nor does it show a promise in writing to the plaintiff as a corporation to pay a certain sum, in installments or otherwise, for the one share of stock set against defendant's name attached to said written contract; nor does said petition of plaintiff's aver any assessments of said share by plaintiff or the board of directors of plaintiff, nor does said petition show that plaintiff had made calls on defendant for installments, or a gross sum payable in installments, nor any necessity for such call. It does not show any amount plaintiff is entitled to recover as a judgment against defendant. It does not show that the amount claimed by plaintiff is now due.

"2. The petition shows the action to be founded on a contract in writing as evidence of indebtedness, and that plaintiff gave defendant notice to pay his subscription agreeably to said subscription, and the by-laws, rules and articles of incorporation of said company, and does not incorporate into and attach to said petition a copy of said by-laws, rules and articles of incorporation of said company, nor does plaintiff state any reason for not doing so."

The demurrer was overruled, and the defendant standing by his demurrer, judgment was rendered for the plaintiff. Defendant appeals.

ADAMS, J.—The defendant insists that the petition is insufficient in that it does not show that any agreement was made with the plaintiff. The agreement, a copy of which is set out, purports to be a subscription to the stock of the Waukon & Mississippi Railroad. The name of the plaintiff is the Waukon & Mississippi Railroad Company. Whether the difference between the two names is such that the petition for that reason might be deemed insufficient we need not determine. No point of that kind is made by the appellant in his argument, and we assume that the point was not designed to be raised by the demurrer. The point urged is that an averment that the defendant signed and delivered to the plaintiff an agreement in writing is not equivalent to an averment that the defendant entered into an agreement with the plaintiff in writing, and if not that the petition is defective. But if a writing which purports to be an agreement is signed and delivered to the promisee as an agreement, it must be regarded as taking effect as an agreement, and this we think is what the petition in this case shows.

It is further insisted by the appellant that the agreement, as set out, contains no promise to pay for the stock; that the promise, if any, is merely implied by law, and that as the petition avers only the signing and delivery of the agreement it avers no promise to pay for the stock.

~~In our opinion the agreement does contain a promise to pay for the stock.~~ The subscription is expressly made subject to the by-laws, rules, and articles of incorporation. Article 4 provides that the stock shall be paid for after five hundred shares have been subscribed, and the petition shows that they have been. (The article becomes as much a part of the contract of subscription as if it had been incorporated directly into the contract.

It is further insisted that the defendant is not a stockholder if he has not paid for his stock, and that if not a stockholder he is not liable to the company. But this position is not well taken. A subscriber to stock becomes a stockholder by virtue of the subscription, in the absence of a provision requiring a payment as a condition of membership; and that, too, without the issuance of any certificate of stock. *Chester Glass Co. v. Dewey*, 16 Mass., 94; *Spear v. Crawford*, 14 Wend., 20; *Vawter v. Ohio & Mississippi R. Co.*, 14 Ind., 174.

It is further insisted that the petition does not show that any assessments have been made. To this it may be said that by article 4 ten per cent of the stock was made payable on the 15th of each month, until the whole is paid as the expenditures require. The petition avers that the expenditures require that the whole stock should be paid. It also avers that the defendant has been duly notified of the requirement.

The object of an assessment, where one is necessary, is to fix the amount that may be called for, and the time when it may be called for. But in the case at bar both amount and time of payment were fixed by the article of incorporation. Nothing remained to be determined but the needs of the company resulting from the expenditures. When the company notified defendant, as the petition avers, that, we think, was a sufficient determination that the expenditures required payment of the stock.

In our opinion the plaintiff's petition is sufficient, and the demurrer was properly overruled.

*Affirmed.*³

³ *Dodge, J.*, in *Smith v. Burns Boiler & Mfg. Co.* (1907) 132 Wis. 177, 111 N. W. 1123: "A subscriber for stock who has been so accepted is completely a stockholder, whether he has paid his subscription or not." But *cf.* *Chase v. Sycamore etc. R. Co.* (1865) 38 Ill. 215.

As to the nature of the liability for subscriptions, see *Commercial Bank v. Warthen* (1904) 119 Ga. 990, 47 S. E. 536, ("The liability of a stockholder upon his stock subscription depends upon the contract of subscription. There would seem to be no room for question that the right of the corporation to enforce the payment of subscriptions is one arising upon contract."). See also *Mississippi etc. R. Co. v. Gaster* (1859) 20 Ark. 455.—Eds.

BALTIMORE, ETC., R. CO. v. HAMBLETON.

1893. 77 Md. 341, 26 Atl. 279.

APPEAL from the Circuit Court No. 2 of Baltimore City. The case is stated in the opinion of the Court.

McSHERRY, J., delivered the opinion of the Court.

By chapter 71 of the Acts of 1862 the Baltimore City Passenger Railway Company was incorporated. Its capital stock was limited to forty thousand shares, which in the course of a few years were fully paid up. The Act of 1890, ch. 271, made provision for the substitution of some other motive power in the place of horses, which were then used to draw the company's cars, and authority was given to the company by the Legislature to raise the money needed to effect this change, and to defray the expense of providing rapid transit. The company was accordingly authorized to increase its capital stock, but not beyond two hundred and forty thousand shares, and also to borrow upon bonds secured by mortgage an amount of money not exceeding its authorized capital stock. The Act declares that "all new or additional stock * * * shall be paid for in money as and when the board of directors" shall call for the same, and that "all the shareholders of the said company shall have the privilege of subscribing for said new or additional stock, ratably and in proportion to their respective holdings," paying therefor the par value thereof. Under the Act of 1890 the shareholders, at a meeting held in July of that year, authorized the issue of forty thousand shares of new or additional stock, of the par value of twenty-five dollars per share, to be paid for in money as and when the board of directors should call for the same; and, following the directions of the Act, made provision for the shareholders to subscribe within a designated time for their respective ratable proportions thereof. Public notice was given of this action, and a circular containing the same information was sent to each shareholder.

Miss Cordelia D. Hollins was then the owner of eighty-five shares of the original stock, and electing to avail of the privilege accorded to the holders of that stock of subscribing to the new stock, caused her name to be entered in the company's subscription book by her brokers, McKim and Company, as a subscriber for eighty-five shares of the new or additional stock. Subsequently Miss Hollins died, and her executor sold to the appellee, John A. Hambleton, the eighty-five shares of original stock standing in her name, and these shares were duly transferred on the books of the railway company to the purchaser. Mr. Hambleton claimed, that by virtue of his ownership of these shares of the original stock he became likewise the owner of the eighty-five shares of new stock for which Miss Hollins had subscribed, and that he was entitled to have these new shares transferred to him on the books, and to have a certificate issued to him showing him to be the owner of them, subject to the right of the

company to exact from him the payment of the par value thereof. The railway company refused to make the transfer or to issue the certificate, and he thereupon filed a bill of complaint in Circuit Court Number Two of Baltimore City, praying for an injunction against the company, requiring it to make the transfer and to issue the certificate. After the company had answered and considerable testimony had been taken the case was heard and an affirmative injunction was directed to issue as prayed. From that decree the pending appeal was taken.

It will be observed that the shares in controversy are not part of the original stock of the company; they are some of the new or additional stock, and the distinction between these two classes—between original or formative stock and subscriptions for new stock, which a corporation after its organization has been authorized to issue—is important in its bearing on the decision of the principal question involved in this cause. There is a substantial difference between an increase of capital and a filling up of one both authorized and required. *Curry vs. Scott*, 54 Pa. St., 276. When the subscription to formative stock precedes the creation of the body corporate which will ultimately issue the certificates, there is, of necessity, at the time such subscriptions are entered into, no corporation in existence with which a contract could be made. The subscribers, as a consequence, and for the very purpose of effecting an organization, become stockholders by the mere act of subscribing if there are no conditions precedent prescribed, and they are thereby invested with the privileges and subjected to the liabilities incident to that relation. The subscribers, in the absence of any statutory restrictions, acquire by such a subscription an interest in the body corporate and a right to participate in its organization. They all stand upon the same footing, incurring the risks and hazards of a failure of the enterprise or sharing its profits in proportion to their interests, and to give vitality to the artificial entity they must become stockholders immediately upon becoming subscribers, if no other method be provided in the charter. But the same reasons do not apply, and the same conditions do not obtain, in the case of new or additional stock authorized to be issued by an existing and completely organized corporation. A subscription to such new stock does not necessarily of itself make the subscriber a stockholder, because, generally speaking, it is a mere contract between the subscriber and the corporation. If by a mere subscription for new stock the subscriber becomes a stockholder, he at once becomes clothed with all the rights of a stockholder, and without the payment of a dollar he would be at liberty to vote his stock, and entitled to claim dividends upon it. As between shareholders of the same class there can be no discrimination, and profits set aside for dividends must be evenly divided amongst the stockholders according to the amount of stock each one owns. *Harrison vs. Mexican Railway Co., L. R.*, 19 Eq. Cases, 358. Hence the policy of a corporation might be molded or controlled by mere sub-

scribers, who have paid nothing upon their subscriptions, to the prejudice or loss of the full paid shareholders, whose money, contributed in the beginning, had actually developed the enterprise. Part of the stock would then be full paid and the rest would be stock upon which nothing had been paid—and yet the latter would possess all the advantages, privileges and incidents which belong to the former, and might be so managed as to render the paid up stock wholly or partially valueless. Whilst it has been held that stockholders who have partially paid for, but have not been called upon to pay up their stock in full, are entitled, when dividends have been declared, to participate therein equally with shareholders whose stock has been entirely paid for, *Oakbank Oil Co. vs. Crum*, L. R., 8 App. Cases, 65, still a *mere subscriber* for stock can claim no such right.

To constitute a subscriber for new stock a stockholder something more than a mere subscription is requisite—*payment* is necessary. The subscription is but the contract; *payment*, when called by the company and when made by the subscriber, constitutes him a shareholder whether a certificate has been issued or not. *Fulgam vs. Macon & Brunswick R. R. Co.*, 44 Ga., 597; *Terwilliger vs. G. W. Tel. Co. et al.*, 59 Ill., 249; *Johnson vs. Albany & Susq. R. R. Co.*, 54 N. Y., 416; *Jay Gould vs. Town of Oneonta*, 71 N. Y., 298. In *Pacific Nat. Bk. vs. Eaton*, 141 U. S., 234, it was shown that the bank had resolved to double its stock and that the original shareholders were given the opportunity to take the new stock in the same proportion in which they held the old. Mary J. Eaton subscribed for forty shares—that being the number of her original shares—paid the full par value thereof and was furnished with a receipt acknowledging the payment “on account of subscription to new stock.” The bank did not succeed in getting the whole issue of new stock taken, and with the consent of the Comptroller of the Currency, reduced the amount of the proposed new stock to the quantity actually subscribed, some forty thousand dollars less than the full increase originally intended. Subsequently Mary J. Eaton sued to recover back from the bank the money she had paid, and founded her claim upon the contention that her subscription was conditional upon the whole amount of new stock being taken; but the Supreme Court, reversing the Supreme Judicial Court of Massachusetts, held that she could not recover the money back, and that she had become a stockholder by subscribing and *paying* the price of the stock. Speaking through the late Mr. Justice Bradley, the court said: “The case is not like that of a deed for lands, which has no force and is not a deed, and passes no estate, until it is delivered. In that case everything depends on the delivery. But with capital stock it is different. Without express regulation to the contrary, a person becomes a stockholder by subscribing for stock, paying the amount to the company or its proper officer and being entered on the stock book as a stockholder.” Indeed, this has been distinctly so decided by this Court in *Busey, et al. vs. Hooper, et al.*, 35 Md., 15. In that case it appeared that Busey,

Bankard and McCurley subscribed for a majority of the shares of the capital stock of the Citizens' Railway Company, but did not make a payment of five dollars per share when subsequently called on therefor; that the other subscribers met pursuant to notice, and elected officers and organized the company, whereupon Busey, Bankard and McCurley claiming to have a majority of the stock, filed a bill in equity against these other subscribers alleging that these other subscribers had conspired and confederated together for the purpose of defrauding the complainants out of their just rights as stockholders, and that the pretended election was part of the machinery by which the defendants designed to accomplish the said fraud. The bill then prayed for an injunction to restrain the defendants from intermeddling in any way with the business or affairs of the Citizens' Railway Company and for the appointment of a receiver. In the argument it was insisted "that by virtue of their subscription to the stock of the corporation, the complainants became owners of the amount of stock subscribed for by them, and entitled to all the rights and privileges of stockholders; and such subscriptions made them members of the corporation and entitled to vote at elections." But this Court, in affirming the order dissolving the injunction, said: "None of the cases decide that the mere fact of subscribing to the stock of an incorporated company constitutes the subscriber a stockholder, but that such subscription puts it in his power to become a stockholder by compelling the corporation to give him the legal evidence of his being a stockholder, upon his complying with the terms of the subscription." In *St. Paul, Stillwater and Taylor's Falls R. R. Co. vs. Robbins*, 23 Minn., 439, it was shown that Robbins had subscribed for preferred stock of the company; that this was not original or formative stock; that there had been no call or assessment upon the subscribers nor any demand for payment, but the company sued on the subscription and the question was whether the suit could be maintained. The Court said: "It appears from the complaint, that at the time of this subscription, the company was fully organized, so that it does not stand upon precisely the same footing as a subscription made prior to, and for the purpose of effecting, the organization. Such a subscription gives to the subscriber an interest in the corporation, and the right to take part in organizing it, and this interest and right are a sufficient consideration to support his promise. But the subscription in this case does not appear to have been to the original stock; on the contrary, it appears that, after the company was fully organized its board of directors authorized and directed the issuance of what, in the amended complaint, is called 'preferred capital stock,' and also directed that the company's books should be opened to receive subscriptions for the same. The mere subscription to this stock, while it constitutes a valid contract on the part of the company to issue the stock to defendant upon his paying for it, and, on his part, to receive and pay for it, does not give him an interest in the company, nor vest in him the title to the stock."

The sale by Miss Hollins' executor of the eighty-five shares of old stock carried with it as an incident the right which the testatrix had previously acquired by virtue of her subscription, to purchase eighty-five shares of the new stock, and the appellee has under the transfer made to him precisely that right and none other. The terms upon which the subscription was made by Miss Hollins are binding upon the appellee as they were upon her. Payment of the par value in money, at the times and in the installments to be named by the directors, must be made before the title will pass. The subscriber binds himself to pay when requested, and the company in turn undertakes upon receiving payment to enter him as a stockholder on its books. Until this is done the contract is executory, and neither the subscriber nor his assignee is a stockholder, and consequently neither is entitled to a certificate of stock or to any other instrument indicating ~~that he is the owner of the shares~~. The obligation he assumes to pay for the stock enures under sec. 64, Art. 23 of the Code, to the benefit of creditors of the corporation, but does not give him a beneficial interest in the body corporate as an owner of its stock until the stock has been paid for.

Mr. Morawetz in his work on Private Corporations has criticised the Minn. Cases and the case in 71 N. Y., but we think they accord fully with Busey's Case in 35 Md., and are not in conflict with any adjudged cases to which we have referred. The decisions chiefly relied on by the appellee arose out of subscriptions to original or formative stock, and are for that reason distinguishable from the case at bar. We do not deem it necessary to review them, but our examination of them has satisfied us of the existence of this broad difference.

The decree of the Court below directed an injunction to issue as prayed, but for the reasons we have given, that decree was erroneous, and must be reversed. And as Mr. Hambleton will not be entitled to any certificate until he becomes a stockholder as to these new shares, none of the relief sought under the bill can be granted, and the bill will, therefore, have to be dismissed.

Decree *reversed*, and bill dismissed, with costs above and below.*

* Cf. *Scott v. Latimer* (1898) 89 Fed. 843, 33 C. C. A. 1, *affd. sub nomine*, *Scott v. Deweese* (1900) 181 U. S. 202, 21 Sup. Ct. 585. See also *Minneapolis Harvester Works v. Libby* (1877) 24 Minn. 327, and discussion in *I Morawetz, Priv. Corps.*, § 61.

That a subscriber to shares, which constitute portion of an increase in capital stock, may become subject to the statutory liability to creditors of a shareholder, before payment in full for his shares, see *Booth v. Campbell* (1872) 37 Md. 522.—Eds.

Section 2.—Requisites of Validity—Defenses.**HUDSON REAL ESTATE CO. v. TOWER.**

1892. 156 Mass. 82, 30 N. E. 465.

CONTRACT to recover the amount of a subscription by the defendants, who were copartners, toward the erection of a factory. At the trial in the Superior Court, before Hammond, J., it appeared that the defendants signed the subscription paper in question. In defence they offered to show that one Harriman, as a solicitor of subscriptions for the capital stock of the corporation which was to be formed at some time after the subscription was made, asked the defendant Herman C. Tower to subscribe; that Tower said that, if the subscribers were going to mortgage the property to be bought with the subscriptions, his subscription would be merely nominal, but that if they would raise the full amount by subscription and not mortgage the property he would subscribe for ten shares, or five hundred dollars' worth; that Harriman thereupon asked him to subscribe with that understanding, but he declined to do it; that, Harriman urging again that he should subscribe upon that understanding, Tower said that he would put down his name if it was understood between them that that was the condition of his subscription, and upon this assurance from Harriman he did subscribe at the time for that amount; that thereafter Harriman reported to the meeting of the subscribers the condition of the defendants' subscription, and that in consequence of that report the meeting voted "that there shall be no mortgage on the property"; that thereafter, and before anything was done by the subscribers, one of them, then active in their affairs and later president of the corporation, informed Tower that they intended to rescind the vote whereby they voted not to mortgage; that thereupon Tower told this gentleman that, if they so voted, he wouldn't pay a penny of his subscription; that this information had come to the ears of a number of the subscribers; that thereafter, namely, upon August 31, 1889, they voted, "that the vote whereby we voted, August 14, 1889, not to place a mortgage on the property, be rescinded"; that thereafter the subscribers formed a corporation, and the corporation did, on April 1, 1890, place a mortgage for \$17,000 upon the property. The defendants further offered to show that nothing had been done by the subscribers, in consequence of the subscriptions, before the revocation by the defendants.

The court ruled that this would not constitute a defence, and directed a verdict for the plaintiff; and the defendants alleged exceptions.

ALLEN, J.—At the time when the defendant signed the subscription paper declared on, it was not a contract, for want of a contracting party on the other side; but it has now been established that a subscription of this sort becomes a contract with the corporation

when the corporation has been organized, and in this way the objection of the want of a proper contracting party is finally avoided, provided everything goes on as contemplated without any interruption. Until the organization of the corporation, the subscription is a mere proposition or offer, which may be withdrawn, like any other unaccepted offer. Unless the signer is bound upon a contract, he is not bound at all. It is open to him to withdraw. It is not on the ground that there was no sufficient consideration. The seal would do away with any doubt on that score. But it is on the ground that for the time being and until the corporation is organized the writing does not take effect as a contract, because the contemplated party to the contract, on the other side, is not yet in existence, and for this reason, there being no contract, the whole undertaking is inchoate and incomplete, and since there is no contract, the party may withdraw. *Limerick Academy v. Davis*, 11 Mass. 113. *Thompson v. Page*, 1 Met. 565. *Ives v. Sterling*, 6 Met. 310. *Perkins v. Union Button-Hole & Embroidery Machine Co.* 12 Allen, 273. *Athol Music Hall Co. v. Carey*, 116 Mass. 471. *Phipps v. Jones*, 20 Penn. St. 260.

In the present case, there was evidence which would warrant finding that the defendant thus withdrew, before the time came when his subscription would have become a contract.

*Exceptions sustained.*¹

AVON SPRINGS SANITARIUM CO. v. WEED.

1907. 119 App. Div. (N. Y.) 560, 104 N. Y. S. 58.

APPEAL by the defendant, William J. Weed, from an interlocutory judgment of the Supreme Court in favor of the plaintiff, entered in the office of the clerk of the county of Livingston on the 29th day of

¹ As to sufficiency of notification of withdrawal of subscription, see same case on later appeal, (1894) 161 Mass. 10, 36 N. E. 680.

Accord, *Knox v. Childersburg Land Co.* (1888) 86 Ala. 180, 5 So. 578; *Richelieu Hotel Co. v. International Military Encampment Co.* (1892) 140 Ill. 248, 29 N. E. 1044 (sufficiency of acceptance); *Bryant's Pond Steam-Mill Co. v. Felt* (1895) 87 Maine 234, 32 Atl. 888; *Athol Music Hall Co. v. Carey* (1875) 116 Mass. 471; *Plank's Tavern Co. v. Burkhard* (1891) 87 Mich. 182, 49 N. W. 562; *Sedalia &c. R. Co. v. Wilkerson* (1884) 83 Mo. 235; *Ashuelot Boot & Shoe Co. v. Hoit* (1876) 56 N. H. 548; *Buffalo etc. R. Co. v. Gifford* (1882) 87 N. Y. 294; *Muncy Traction Engine Co. v. DeLaGreen* (1888) 143 Pa. St. 269, 13 Atl. 747; *Badger Paper Co. v. Rose* (1897) 95 Wis. 145, 70 N. W. 302; *McNaught v. Fisher* (1899) 96 Fed. 168, 37 C. C. A. 438; *Doherty v. Arkansas etc. R. Co.* (1905) 142 Fed. 104, 73 C. C. A. 328.

"The only question we find it necessary to consider is whether a subscriber to the capital stock of an unorganized corporation has a right to withdraw from the enterprise, provided he exercises the right before the corporation is organized and his subscription is accepted. We think he has. Such a subscription is not a completed contract. It takes two parties to make a contract. A non-existing corporation can no more make a contract for the sale of its stock than an unbegotten child can make a contract for the purchase

January, 1907, upon the decision of the court, rendered after a trial at the Monroe Special Term, overruling the defendant's demurrer to the complaint.

WILLIAMS, J.—The interlocutory judgment should be affirmed, with costs, with leave to plead over upon payment of the costs of this appeal and of the demurrer.

The action was brought to recover the amount of a subscription for stock in the plaintiff corporation.

The ground of the demurrer was that the complaint did not allege facts sufficient to constitute a cause of action.

The complaint alleged that the plaintiff was a domestic corporation, organized with a capital stock of \$40,000, of which \$25,000 was seven per cent preferred, of the par value of \$50 per share; that the defendant and certain other persons, on or about October 26, 1905, in contemplation of the incorporation of the plaintiff, made and subscribed an agreement in writing as follows: "I hereby subscribe for 10 shares of 7 per cent preferred stock, at \$50 per share, par value \$50, in a new company to be formed for the purpose of purchasing and carrying on the Avon Springs Sanitarium, to be known as the Avon Springs Sanitarium Company, or a name to be selected. It is understood and agreed that this stock is fully paid and nonassessable, I to receive seven per cent dividends upon the above number of shares to be paid the 1st day of January of each and every year commencing January 1, 1907. I agree to pay for the above number of shares of stock as soon as the company is incorporated and upon delivery of stock to me." that on or about December 1, 1905, the plaintiff was organized as before alleged for the purpose of conducting a sanitarium and the business connected therewith; that plaintiff, after incorporation, accepted the defendant's subscription for stock, and relying thereon, purchased the Avon Springs Sanitarium and began to carry on the same and has continued to carry it on; that the defendant was notified that the stock subscribed for by him was ready for delivery, and delivery of the certificate for such stock was tendered to defendant before the commencement of this action and on October 30, 1906; that the defendant has at all times omitted to pay for the stock, and then judgment was demanded for \$500, with interest from October 30, 1906.

When this action was commenced and the complaint was served, the certificate of incorporation had been made and filed and the plaintiff had been incorporated and was in existence. The contents of the certificate were not alleged, and it was not annexed to or made a part of the complaint. We do not know what the contents of the certificate or the details of the organization of the incorporation

of it." Walton, J., in *Bryant's Pond Steam-Mill Co. v. Felt*, (1895) 87 Maine 234, 32 Atl. 888.

As to the effect of death or insanity of the subscriber, see *Beach v. First M. E. Church* (1880) 96 Ill. 177; *Sedalia &c. R. Co. v. Wilkerson* (1884) 83 Mo. 235; *Wallace v. Townsend* (1885) 43 Ohio St. 537.—Eds.

were. If the complaint was indefinite and uncertain for these reasons, the proper remedy was by motion to make it more definite and certain. We must assume that it was legally and properly incorporated, and that the certificate contained the necessary information required by the statute. The complaint alleges that the agreement subscribing for stock was made in contemplation of the incorporation of the plaintiff; that is, they made the agreement understanding that the corporation was to be organized just as this plaintiff had been organized, and existed when the complaint was served. This allegation and these facts are admitted by the demurrer. A different condition of things may appear when a trial is had and all the facts are made to appear. Upon the facts as admitted by the demurrer we think a good cause of action existed. The appellant claims the agreement was not binding upon the defendant and could not be enforced under the law applicable to such agreements. Morawetz on Corporations (2d ed.) states the law as follows: (§ 47) "If a number of persons mutually agree to become shareholders in a corporation to be formed by them subsequently, either under a special charter or under some general law, the agreement between the parties is originally made up of a series of ordinary common law contracts. If the parties intend to become shareholders, without further act on their part, immediately after the incorporation of the company, their agreement may very properly be held to include a continuing offer to become shareholders as soon as the corporation shall be formed. (This offer may be accepted by the corporation, through its regular agents, after organization, unless previously revoked; by such acceptance the contract of membership is consummated, and the parties become stockholders in the corporation, with all the resulting rights and liabilities;)" (§ 49) "A different case is presented where the parties mutually agree to subscribe for shares in a corporation to be formed thereafter. Here there is no unconditional agreement to become shareholders as soon as the corporation shall be formed, but it is contemplated that the parties shall themselves perform an additional act before becoming shareholders; namely, execute the statutory contract of membership by subscription upon the stock-books. It is plain, therefore, that in this case there is no offer which the corporation can accept, and the parties do not become stockholders, and cannot be charged as such, unless they subsequently carry out their agreement by subscribing for the shares."

Buffalo & Jamestown R. R. Co. v. Gifford (87 N. Y. 294) is an illustration of the rule under section 47 (supra), and Lake Ontario Shore R. R. Co. v. Curtiss (80 id. 219) is an illustration of the rule under section 49 (supra).

In the Curtiss case the agreement was to subscribe for stock in the future, and in the opinion the court say: "It is, therefore, not a subscription to the capital stock of the plaintiff, taking effect presently, but a promise, each subscriber with the other, to do so at some future time. * * * If any action could be maintained upon it by

any person, it must be some one of the subscribers or his assignee. The legal effect of the contract is restricted to them. * * * When two persons for a consideration sufficient as between themselves covenant to do some act which if done would incidentally result in the benefit of a mere stranger, that stranger has not a right to enforce the covenant, although one of the contracting parties might enforce it as against the other. As to the plaintiff the contract is purely voluntary, and without consideration."

In the Gifford case the agreement was a present subscription for the stock, and it was held valid and enforceable by the corporation. The court said: "While the subscription was not valid and binding before the complete formation of the corporation, because there was no party with whom the defendant could then contract, yet after the corporation was formed, it accepted the subscription and recognized the defendant as a stockholder, and he recognized himself as a stockholder and ratified and confirmed his subscription by payments thereon. He thus, within all the authorities, upon general principles, became a stockholder in the company, liable to pay the full amount of his subscription. * * * In that (the Curtiss) case, the contract sued upon was *not* one of subscription to plaintiff's stock. It was simply a promise that the defendants would subscribe," etc.

The principle that a subscription for stock, before the corporation is formed, may be enforced by the corporation after it comes into existence is recognized in many cases in this state and seems never to have been questioned. (Louisville & B. R. R. Co. v. Elliot, 101 N. Y. Supp. 328.) (See Schenectady & Saratoga Plank Road Co. v. Thatcher, 11 N. Y. 102; Buffalo & Pittsburgh R. R. Co. v. Hatch, 20 id. 161; Buffalo & N. Y. City R. R. Co. v. Dudley, 14 id. 336; Stanton v. Wilson, 2 Hill, 153; Non-Electric Fibre Mfg. Co. v. Peabody, 21 App. Div. 247; Yonkers Gazette Co. v. Taylor, 30 id. 334.)

* * * * *

Our conclusion is that the judgment appealed from should be affirmed.

All concurred, except McLENNAN, P. J., who dissented in an opinion.

McLENNAN, P. J. (dissenting):

The question presented by this appeal is a simple one, and, as it seems to me, has been decided adversely to respondent by the courts of this State, and that it is only necessary to appreciate the precise facts in order to reach a conclusion in harmony with such decisions.

If a cause of action exists in plaintiff's favor against the defendant, it must result because of the alleged contract set out in full in the complaint and in the prevailing opinion, and which need not be repeated here. Its provisions, so far as material, are: "I (the defendant) hereby subscribe for 10 shares of 7 per cent preferred stock * * * in a new company to be formed for the purpose * * *. I agree to pay for the above number of shares of stock as soon as the company is incorporated and upon delivery of stock to me."

If such alleged contract does not impose an obligation upon the defendant which the plaintiff may enforce, the complaint fails to state a cause of action, and it is idle to consider what inferences might be drawn from the other allegations of such complaint, because the terms of such alleged contract are not ambiguous; and, therefore, may not be varied, changed or given greater scope by parol evidence.

So far as appears there was no person other than the defendant a party to such alleged agreement. No one is suggested who was under obligation to or could return any advantage or consideration to the defendant for the obligation which it is claimed he assumed. It is said that the plaintiff became the beneficiary of such obligation, but if so it would seem essential that some one should be authorized to confer such rights upon it. So far as appears, persons who were utter strangers to the defendant may have organized the corporation by the name and for the purposes contemplated by him; but we cannot imagine that such persons, without the knowledge or consent of the defendant, would be competent to form such corporation and then through it to enforce defendant's alleged agreement. With whom the defendant contracted, if at all, does not appear. There is no party of the second part named in the alleged agreement; no one upon whom he could call to perform the covenants or agreements which formed the only consideration for his alleged obligation. The defendant did not agree to form the plaintiff corporation, nor did he authorize any one to form it for him or on his behalf.

It is well settled that if two or more persons mutually agree to organize a corporation and each subscribes for stock therein to be paid for after its incorporation, such agreement is valid and may be enforced by any of the parties thereto or by the corporation after its formation. In such case the corporation represents and acts for the parties to the agreement, is their agent. (But, we think, it has never been held by the courts of this State that a subscription to the stock of a corporation could be enforced where there was no agreement to incorporate and where there were no parties between whom mutuality of agreement existed.)

In *Woods Motor Vehicle Co. v. Brady* (181 N. Y. 145) the agreement which was sought to be enforced was as follows: "We, the undersigned, in consideration of the mutual covenants and agreements hereinafter contained, hereby subscribe for the number of shares set opposite our respective names, of the seven per cent. preferred, non-cumulative capital stock of a corporation to be organized under the laws of the State of New York, for the purpose of dealing in automobiles and motor vehicles, which corporation is to have a capital stock of three hundred thousand dollars (\$300,000), of which one hundred thousand dollars (\$100,000) shall be seven per cent (7%) preferred, non-cumulative stock, and two hundred thousand dollars (\$200,000) common stock, and we further agree to pay for the said stock so subscribed, whenever payment of the same may be called for by the Board of Directors of said corpora-

tion." Judge Vann, in delivering the opinion of the court, said (p. 152): "The plaintiff was not a party to the subscription paper which was signed by eight persons and which, if capable of enforcement at all, could be enforced only by one of the contracting parties against another." In that case it was pointed out that the paper could not be enforced at all for other reasons which it is unnecessary to consider here.

In *Yonkers Gazette Co. v. Taylor* (30 App. Div. 334) it is said that in order to give validity to such subscription paper there must be an agreement to form a corporation. Mr. Justice Hatch, in writing the opinion for the court in that case, said (p. 336): "The law is fairly well settled that where parties propose to form a corporation and become shareholders therein, and such parties intend to become such shareholders without further act upon their part, upon the incorporation of the company, and the agreement remains open and is unrevoked and the corporation is formed in pursuance of it and thereafter acts upon it by accepting the same, such agreement is valid and binding as a subscription to the capital stock of such corporation. * * * There are agreements of a somewhat similar character which do not admit of enforcement and are not binding as a common-law agreement. It is quite easy to confuse the two classes, although there is a clear distinction between them. (In the first class it is to be noticed that the agreement is to form a corporation and subscribe to its stock. The latter class are mutual agreements to subscribe for stock in a corporation thereafter to be formed., In the first the agreement is unconditional and absolute to form the corporation and take the stock, and when acted upon by the corporation is binding, as that is all that is needful to make the contract of force."

The same rule is stated in *Morawetz on Corporations* (2d. ed. § 47) where it is said: "If a number of persons mutually agree to become shareholders in a corporation to be formed by them subsequently, either under a special charter or under some general law, the agreement between the parties is originally made up of a series of ordinary common-law contracts," and the author says that such agreements may be enforced by the corporation after its formation.

In *Lake Ontario Shore R. R. Co. v. Curtiss* (80 N. Y. 219) the agreement which was being considered was as follows: "We the undersigned, citizens of Unionville and vicinity, pledge ourselves to subscribe for and take stock in and for the construction of the Lake Ontario Shore Railroad to the amount set opposite our names respectively, on condition said road be located and built through or north of the village of Unionville in Parma." In an action brought to enforce such agreement it was held that it was not a subscription to plaintiff's capital stock; that it (the plaintiff) was in no sense a party to the agreement and could not maintain an action thereon. It was further held that when two persons for a consideration sufficient as between themselves, covenant to do some act which, if done, would incidentally result in the benefit of a mere stranger, that

stranger has not a right to enforce the covenant, although one of the contracting parties might enforce it as against the other.

The case of *Buffalo & Jamestown R. R. Co. v. Gifford* (87 N. Y. 294) is not authority for respondent's contention. In that case the defendant with other persons signed an agreement in writing by which they each agreed to take the number of shares "of the capital stock of said company set opposite our respective names, and agree to pay therefor in such time and manner as required by said company." In that case the Court said (p. 299): "While the subscription was not valid and binding before the complete formation of the corporation, because there was no party with whom the defendant could then contract, yet after the corporation was formed, it accepted the subscription and recognized the defendant as a stockholder, and he recognized himself as a stockholder and ratified and confirmed his subscription by payments thereon. He thus, within all the authorities, upon general principles, became a stockholder in the company, liable to pay the full amount of his subscription."

In the case at bar if the defendant had ratified the acts of the parties who formed the plaintiff corporation, no one would pretend that the payment of his subscription could not be compelled by such corporation.

In *Buffalo & N. Y. City R. R. Co. v. Dudley* (14 N. Y. 336) the defendant with others signed the following: "We, the subscribers, agree to take the number of shares by us subscribed of the capital stock of the Attica and Hornellsville Railroad Company, subject to all the liabilities and penalties of the charter and by-laws of the said corporation." The defendant at the time of signing such agreement paid five per cent upon the amount of stock subscribed for by him and took the receipt of one of the commissioners therefor. It was held that when the defendant had thus subscribed his name and had paid his five per cent and took his receipt therefor it had the effect of making him a stockholder and the owner of the shares subscribed for by him.

In the case of *Schenectady & Saratoga Plank Road Co. v. Thatcher* (11 N. Y. 102) it appeared that the defendant and eight other persons who had subscribed for stock had been duly elected directors of the company for the first year, and that the defendant was present at such election, and acted as superintendent of the company; that he paid five per cent at the time of subscribing for his stock and later an additional installment of ten per cent. And it also appeared that he had transferred fifty shares of his stock to others who had paid him for the same. It was held in that case and for all those reasons that payment for the stock subscribed for by him could be enforced by the corporation.

It is concluded that in order to make a present subscription for stock in a corporation thereafter to be formed valid, there must be an agreement between two or more parties to form such corporation, and that only after its formation by such parties or by some one au-

thorized to act for them in that regard can their subscriptions to its capital stock be enforced by such corporation.

We think such rule is reasonable and will prevent the anomalous situation of strangers to a subscription agreement for stock in a corporation to be formed and to the party or parties thereto, organizing such corporation perchance without the knowledge or consent of such subscribers for its stock and then by action brought in its name, compel payment of their subscriptions.

The interlocutory judgment should be reversed and the demurrer to the complaint sustained, with costs.

Interlocutory judgment *affirmed*, with costs, with leave to the defendant to plead over upon payment of the costs of the demurrer and of this appeal.²

NEBRASKA CHICORY CO. v. LEDNICKY.

1907. 79 Neb. 587, 113 N. W. 245.

APPEAL from the district court for Cuming county: Guy T. Graves, Judge. Reversed.

EPPELSON, C.—

In February, 1897, certain citizens of Schuyler, Nebraska, united in a movement for the organization of a company for the manufacture of chicory at that place. Articles of incorporation were prepared and discussed on one or more occasions by the interested parties, and during said month a written agreement, of which the following is a copy, was prepared and circulated and signed by a considerable number of persons, the signature of the defendant being attached thereto as below indicated: "We the undersigned do hereby agree to take shares of stock in the Nebraska Chicory Company of Schuyler, Nebraska, to be organized on the plan set forth in the articles of incorporation, and we agree to pay for the number of shares set opposite our respective names in accordance with the by-laws, rules and regulations of the company, which provide for a division of the capital stock of \$50,000 in shares of \$50 each, to be paid in monthly installments of 4 per cent. per month, beginning on the first Saturday of March, 1897. (Signed.) Anton Lednicky, 5 shares." Some time after the defendant signed the foregoing, and on or about March 8, 1897, a certificate of incorporation was filed with the county clerk, and with the secretary of state on March 25.

² Reversed on dissenting opinion of McLennan, P. J., below, *Avon Springs Sanitarium Co. v. Kellogg* (1907) 189 N. Y. 557, 82 N. E. 1123.

Cf. Avon Springs Sanitarium Co. v. Kellogg (1908) 125 App. Div. (N. Y.) 51, 109 N. Y. S. 153; *affd. short, sub nomine, Smith v. Kellogg* (1909) 194 N. Y. 567, 88 N. E. 1132.—Eds.

Section 4138, Ann. St., provides that upon this latter filing the organization should be deemed completed and the persons whose names are subscribed thereto be deemed a body corporate. Section 4140 is as follows: "The persons named in the certificate of incorporation, or a majority of them, shall be commissioners to open the books for the subscription to the capital stock of said company, and at such time and places as they shall deem proper, and the said company are authorized to commence operations upon the subscription of ten per cent. of said stock." No stock subscription book, other than the paper above set out, was opened by the authority of the corporation, but that body proceeded to transact business by the purchase of grounds and the erection of buildings and supplying the same with fixtures and machinery, chicory, etc., and the defendant, for eight months consecutively, paid into its treasury monthly instalments of \$10 each pursuant to the terms of his agreement. On June 29, 1897, the president and secretary executed and delivered to him a paper certifying that he had subscribed for five shares of the capital stock of the company and would be entitled to the same "upon the surrender of this certificate and compliance with the rules and by-laws of this company." For this "certificate of entitlement," as it was called, he subscribed and delivered to the company a written receipt. He ceased to pay on and after the ninth instalment, and this is an action to recover the unpaid residue upon his promise of subscription above copied. At the close of plaintiff's evidence the court directed a verdict for defendant. Plaintiff appeals.

The principal question for determination is whether the written agreement for subscription to the capital stock of the corporation is a contract which the corporation can enforce? It appears that more than 10 per cent. (about \$20,000) of the capital stock had been subscribed before the company began business; that the paper signed by defendant and other subscribers was the only subscription book used or kept by the company; that defendant signed the instrument before the time of the filing of the articles of incorporation, and had paid \$80 on his subscription before this suit was instituted. It was held in *Bolton v. Nebraska Chicory Co.*, 69 Neb. 681, that this identical corporation is a manufacturing corporation, the court saying: "The statute here in question was obviously designed to encourage the promotion of manufacturing enterprises of all kinds, in the widest sense, by relaxing the rules as to organization. There is every reason for giving it a liberal construction, and no fraud can result from so doing."

Defendant contends, however, that one who signs the subscription paper, whereby he agrees to take a certain number of shares in a corporation thereafter to be formed, does not become liable as a shareholder, even after the corporation is formed, and the corporation cannot maintain an action against him upon subscription paper. There are courts, notably Kansas, Massachusetts, Michigan, Pennsylvania and West Virginia, which hold to this doctrine. *Nemaha*

Coal and Mining Co. v. Settle & Keith, 54 Kan. 424; Hudson Real Estate Co. v. Tower, 161 Mass. 10; Schurtz v. Schoolcraft & T. R. Co., 9 Mich. 269; Northern C. M. R. Co. v. Eslow, 40 Mich. 222; International F. & E. Ass'n v. Walker, 88 Mich. 62; Plank's Tavern Co. v. Burkhard, 87 Mich. 182; Muncy Traction Engine Co. v. Green, 143 Pa. St. 269; Auburn Bolt and Nut Works v. Shultz, 143 Pa. St. 256; Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 738. See decisions cited in 10 Cyc. 385, note 97, and 386, note 99. Also Thrasher v. Pike County R. Co., 25 Ill. 393; Sedalia, W. & S. R. Co. v. Wilkerson, 83 Mo. 235; Coyote Gold & Silver M. Co. v. Ruble, 8 Or. 284.

The doctrine of these cases cannot be regarded as settled in American law. "This rule proceeds upon the narrow and strict ground that a contract, such as will bind the intending obligors, must be tendered to the other contracting party, to an artificial being not yet in esse, and in the precise statutory mode, or not at all." 10 Cyc. 386, note 2.

It is said that this court is committed to the rule of the cases above cited, and our attention is called to *Livesey v. Omaha Hotel Co.*, 5 Neb. 50, and *Macfarland v. West Side Improvement Ass'n*, 53 Neb. 417. In *Livesey v. Omaha Hotel Co.*, supra, the sole ground upon which the defendants were held not liable upon their subscription was that the specified amount of capital stock was not subscribed for; and in *Macfarland v. West Side Improvement Ass'n*, supra, the same principle was announced, to wit, that the subscriber was not liable upon his subscription until the capital stock was fully subscribed for, "unless by law or charter provision the corporation is permitted to proceed with its main design with a less subscription." In that case, however, it was held that the defendant was estopped by his conduct to deny his liability. Neither of the above cases have any application to the case at bar, since the statute under which this corporation was formed provides that the corporation may commence operations upon the subscription of 10 per cent. of its capital stock. In *Lincoln Shoe Mfg. Co. v. Sheldon*, 44 Neb. 279, it is held that a contract as follows: "For value received we, the undersigned subscribers, hereby bind ourselves to purchase the number of shares of stock set opposite our respective names in the Lincoln Shoe Manufacturing Company at fifty dollars per share"—upon several conditions recited, was a subscription to the stock of the corporation. This case, however, may be distinguished from the case in hand. In that case, the subscription paper was signed after the articles of incorporation were filed. In the case at bar, it was alleged, and we understand the evidence to show, that the defendant placed his name to the subscription paper prior to the filing of the articles of incorporation. Therefore, whether defendant herein is liable to the corporation on the subscription paper we deem an open question in this state.

Mr. Seymour D. Thompson in his excellent article on "Corporations" in 10 Cyc. 385, et seq., discusses the doctrine for which de-

defendant contends as follows: "The theory of these cases seems to be that if a number of coadventurers mutually agree to subscribe for shares in a corporation thereafter to be formed, this does not amount to an irrevocable contract to become shareholders when the corporation is formed; but they must perform the additional act of executing the statutory contract of membership by signing and acknowledging the articles of association where the corporation is unformed, or by entering their names on its stock-book where it is formed. This theory is that until this additional act is performed there is no offer which the corporation, when formed, or even if already formed, can accept, and that the subscribers do not therefore become shareholders and liable to be charged as such, unless they choose to carry out their agreement by subscribing for the shares. This doctrine, which treats preliminary share subscribers to corporations not yet formed with the utmost levity, which ignores the principle, hereafter explained, that such subscriptions are mutual promises among the subscribers as toward each other, that this mutuality of promise constitutes a sufficient consideration for such a subscription, and that it is none the less so because the promise is made to a third person, the corporation, which is not yet in esse, has been taken up and adopted by a good many modern courts." See "Consequences of Rule." 10 Cyc. 387. In view of the liberal construction given our statute (*Bolton v. Nebraska Chicory Co.*, *supra*), we think the rule for which defendant contends proceeds upon too strict and narrow grounds and should not be adopted in this state. There is good authority for our conclusion. The same learned author further says in 10 Cyc. 388, 389: "Many courts, expressing their reasoning in various ways, have reached the conclusion that a subscription to corporate shares made before the corporation comes into existence, but accepted by the corporation after coming into existence, either expressly by issuing the share certificates, or impliedly by recognizing the subscriber as a shareholder and by extending to him the rights which pertain to that relation, makes him a shareholder. The subscription paper may be informal, yet if the intent of the subscription can be collected from it, as where it states the names and residences of the shareholders, and the number of shares taken by each, it constitutes a subscription to shares of the forthcoming corporation, and the corporation may maintain actions upon it against the signers"—citing *Mahan v. Wood*, 44 Cal. 462; *Glenn v. Busey*, 5 Mackey (D. C.), 233; *Johnson v. Ewing Female University*, 35 Ill. 518; *Tonica & P. R. Co. v. McNeely*, 21 Ill. 71; *Cross v. Pinckneyville Mill Co.*, 17 Ill. 54; *New Albany & S. R. Co. v. McCormick*, 10 Ind. 499; *Nulton v. Clayton*, 54 Ia. 425; *Penobscot R. Co. v. White*, 41 Me. 512; *Penobscot R. Co. v. Dummer*, 40 Me. 172; *Kennebec & P. R. Co. v. Palmer*, 34 Me. 366; *Thompson v. Page*, 1 Met. (Mass.) 565; *Michigan & C. M. R. Co. v. Bacon*, 33 Mich. 466; *Red Wing Hotel Co. v. Friedrich*, 26 Minn. 112; *Ashuelot Boot and Shoe Co. v. Holt*, 56 N. H. 548; *Lake Ontario A. & N. Y. R. Co. v. Mason*, 16 N. Y. 451;

Yonkers Gazette Co. v. Taylor, 30 N. Y. App. Div. 334; *Hamilton & Deansville P. R. Co. v. Rice*, 7 Barb. (N. Y.) 157; *Bell's Appeal*, 115 Pa. St. 88; *Gleaves v. Brick Church Turnpike Co.*, 1 Sneed (Tenn.) 491; *Belton Compress Co. v. Saunders*, 70 Tex. 699.

In *Planters & Merchants I. P. Co. v. Webb*, 39 So. 562 (144 Ala. 666), it was held: "Any agreement by which a person shows an intention to become a stockholder in a corporation is sufficient as a contract of subscription as against both him and the corporation." A subscription by a number of persons to the stock of a corporation to be thereafter formed by them, constitutes a contract between the subscribers themselves to become stockholders when the corporation is formed, upon the conditions expressed in the agreement, and as such it is binding and irrevocable from the date of the subscription. It is in the nature of a continuing offer to the proposed corporation, which, upon acceptance by it, becomes as to each subscriber a contract between him and the corporation. See *Minneapolis Threshing M. Co. v. Davis*, 40 Minn. 110, 3 L. R. A. 796. Such a contract is based upon a sufficient consideration. (Such subscriptions are mutual promises among the subscribers as toward each other, and this mutuality of promise among the subscribers constitutes a sufficient consideration for such a subscription.) There is in the act of the particular subscriber, in subscribing with others, a mutuality of promise which obliges him to make good his promise to the corporation after it comes into its existence. 10 Cyc. 394, note 58, and cases there cited. "Whenever an intent to become a subscriber is manifested, the courts incline, without particular reference to formality, to hold that the contract of subscription subsists. It is, as in the case of other contracts, very much a question of intent. Formal rules are for the most part disregarded. And in general a contract for subscription may be made in any way in which other contracts may be made. Any agreement by which a person shows an intention to become a stockholder is sufficient to bind him and the corporation." 1 Cook, Corporations (5th ed.), sec. 52; 26 Am. & Eng. Ency. Law (2d ed.), 902, 903. "That a subscription for stock implies a promise to pay for it, even though the subscription was before incorporation, is the rule sustained by the great weight of authority." 1 Cook, Corporations (5th ed.), secs. 71, 72, 75; 26 Am. & Eng. Ency. Law (2d ed.), 902; 1 Morawetz, Corporations (2d ed.), secs. 47, 54. We gather this proposition from the decisions and think it is sustained by the weight of authority: A subscription to corporate shares, made before the corporation comes into existence, but accepted by the corporation after coming into existence, either expressly by issuing the share certificates, or impliedly by recognizing the subscriber as a shareholder, makes him a shareholder and the corporation may maintain an action upon the subscription against the signers.

It is argued, however, that the subscription in the case at bar is invalid because not entered by the commissioners in the corporate books as provided by section 4140 Ann. St. As a general rule, "un-

less the charter or governing statute so provides, it is not necessary to the validity of the subscription that it should be originally made in the book prepared for that purpose." 10 Cyc. 392. We believe our statute should be liberally construed, and are of opinion that the true rule is that, although the statute provides for the opening of books, the use of subscription papers in the first instance instead of a book does not make a subscription void. 10 Cyc. 392, citing in note 43: *Brownlee v. Indiana & I. R. Co.*, 18 Ind. 68; *Hamilton & D. P. R. Co. v. Rice*, 7 Barb. (N. Y.) 157; *Ashtabula & L. R. Co. v. Smith*, 15 Ohio St. 328; *Mobile & O. R. Co. v. Yandal*, 5 Sneed (Tenn.), 294; *Stuart v. Valley R. Co.*, 32 Grat. (Va.) 146. "Inasmuch as Acts 1903, p. 310, containing provisions for stock subscriptions, does not provide that unless the specified conditions are complied with a subscription shall not be binding, a subscription is binding, though not formally, or even regularly made." *Planters & M. I. P. Co. v. Webb*, *supra*.

The trial court was in error in directing a verdict for defendant, and we recommend that the judgment be reversed and the cause remanded for a new trial.

By the Court: For the reasons stated in the foregoing opinion, the judgment of the district court is reversed and the cause remanded for a new trial.

*Reversed.**

COPPAGE, RECEIVER, v. HUTTON.

1890. 124 Ind. 401.

FROM the Montgomery Circuit Court.

ELLIOTT, J.—The appellant sues as the receiver of an insolvent corporation, and seeks to recover a subscription which he alleges the appellee made to the capital stock of the corporation. It is alleged that the appellee, with others, signed articles of association, and that he agreed to take two shares of the capital stock, and pay therefor one hundred dollars. The introductory clause of the articles of association reads thus: "We, the undersigned, agree to take the stock in the amount set opposite our names in a company to be organized for manufacturing and selling the Williamson Straw Stacker." There were eighty-three signers, and seven of them acknowledged the ex-

* *Accord*, *Kidwelly Canal Co. v. Raby* (1816) 2 Price (Eng. Excheq.) 93; *Tonica & C. R. Co. v. McNeely* (1859) 21 Ill. 71; *Johnson v. Wabash & Plankroad Co.* (1861) 16 Ind. 389. See also *Cravens v. Eagle Cotton Mills Co.* (1889) 120 Ind. 6, 21 N. E. 981, 16 Am. St. 298; *Lake Ontario & C. R. Co. v. Mason* (1857) 16 N. Y. 451 (*cf.* *Buffalo & C. R. Co. v. Clark* (1880) 22 Hun (N. Y.) 359; *Yonkers Gazette Co. v. Taylor* (1898) 30 App. Div. (N. Y.) 334, 51 N. Y. S. 969).

See note, 8 Columbia Law Rev., 47.—Eds.

execution of the articles of association before a notary public, and the instrument was duly recorded. It is also alleged that eight thousand dollars of stock was subscribed, that the company was duly organized, and a board of directors elected.

There can be no doubt under the authorities that a valid subscription to the capital stock of a corporation may be made by signing the preliminary articles. Such a subscription becomes enforceable upon the perfection of the corporate organization according to law under articles of association. *Miller v. Wild Cat G. R. Co.*, 52 Ind. 51; *Nulton v. Clayton*, 54 Iowa, 425; *Phoenix, etc., Co. v. Badger*, 67 N. Y. 294; *Cravens v. Eagle, etc., Mills Co.*, 120 Ind. 6. If the promise of the appellee is not binding it must be for some other reason than that it was made before the organization of the corporation was fully effected.

The statute requires that the persons who desire to organize a corporation shall "make, sign, and acknowledge, before some officer capable to take acknowledgment of deeds, a certificate in writing," setting forth therein certain enumerated things. Section 3851, R. S. 1881. The contention of the appellee is that the promise is not effective, because the complaint shows that only seven of the eighty-three signers acknowledged the certificate. It seems quite clear, under the decision of this court in *Indianapolis, etc., Mining Co. v. Herkimer*, 46 Ind. 142, that the mere signing of the paper was not sufficient to complete the obligation, and that, in order to make valid and effective articles of association against all who sign, all must acknowledge them as the statute requires. Here it affirmatively appears that seven only of the signers acknowledged the execution of the instrument, and it cannot be inferred that those who did not acknowledge it remained bound by its terms. (As to them the instrument was incomplete, and it is quite well settled that an incomplete subscription can not be enforced.) *Dutchers, etc., R. R. Co. v. Mabbett*, 58 N. Y. 397; *Reed v. Richmond, etc., R. R. Co.*, 50 Ind. 342; *Richmond St. R. R. Co. v. Reed*, 83 Ind. 9; *Williamson v. Kokomo, etc., Ass'n*, 89 Ind. 389.

It is, however, argued by appellant's counsel that the complaint does affirmatively show that the corporation was organized, but this does not meet the question, (for it may well be that it was organized without the appellee as a stockholder). The fact that he did not acknowledge the instrument as the law requires implies that he did not become a stockholder, and there is nothing in the complaint which rebuts or opposes this implication. It devolved upon the plaintiff to remove the inference if he could. As the appellee did not acknowledge the instrument as the law requires, he did not become a stockholder, and if he were insisting that he was entitled to the number of shares set opposite his name, it is quite clear that the corporation might successfully resist his claim, since it is obvious that only those who acknowledge the articles of association as the law requires can successfully insist upon their right to stock. If the appellee can not

The requirement is by statute that all shall sign.

be regarded as a stockholder, then it seems quite clear that he did not bind himself by simply signing the articles of association.

Whether a good complaint can be framed is not the question before us, for the only question presented by the record is as to the sufficiency of the complaint as it is written.

Judgment affirmed.*

CAPPS v. HASTINGS PROSPECTING CO.

1894. 40 Neb. 470, 58 N. W. 956.

ERROR from the district court of Adams county. Tried below before Gastin, J.

RAGAN, C.—

The Hastings Prospecting Company sued Lucius J. Capps and Willis P. McCreary, copartners doing business under the name, firm, and style of Capps & McCreary, in the district court of Adams county on a subscription or writing obligatory signed by them, in words

*The common law rules in respect to the obligations of persons subscribing for stock are binding, "except as they may have been changed by statute, for where the statute prescribes the method of subscription, a subscription made in any other way cannot be enforced." *Planters & Packet Co. v. Webb* (1905) 144 Ala. 666, 35 So. 562. See also *Troy & C. R. Co. v. Tibbits* (1854) 18 Barb. (N. Y.) 297; *Poughkeepsie & C. Plankroad Co. v. Griffin* (1861) 24 N. Y. 150; *Buffalo & C. R. Co. v. Gifford* (1882) 87 N. Y. 294; *General Electric Co. v. Wightman* (1896) 3 App. Div. (N. Y.) 118, 39 N. Y. S. 420; *Ashtabula & C. R. Co. v. Smith* (1864) 15 Oh. St. 328.

In *Hapgoods v. Lusch* (1907) 123 App. Div. (N. Y.) 23, 107 N. Y. S. 331, held that defendant's giving of his note as payment for 10 per cent. of the value of 25 shares of an original issue of stock subscribed to by him was not equivalent to the cash payment of 10 per cent. required by statute, the transaction constituting not a payment but a mere promise to pay, and that, therefore, defendant's subscription was not binding upon him. *Jenks, J., said:* "In this State statutes, not common-law principles, regulate contracts for shareholding in corporations. (*General Electric Co. v. Wightman*, 3 App. Div. 118, 123, 39 N. Y. S. 420.) In this State it is settled that the omission to obey a statutory requirement of a payment in cash upon a subscription makes the subscription invalid and not binding upon the subscriber. (N. Y. & Oswego M. R. R. Co. v. Van Horn, 57 N. Y. 473; *Cook Corp.* [5th ed.], § 174; *South Buffalo Natural Gas Co. v. Bain*, 9 Misc. Rep. 425, 30 N. Y. Supp. 264, citing authorities.) The giving of the note was not the equivalent of a cash payment of 10 per cent. In *Excelsior Grain Binder Co. v. Stayner*, (25 Hun 91) and in *Durant v. Abendroth*, (69 N. Y. 148, 25 Am. Rep. 158,) the reasoning which rejected checks as equivalent to cash is applicable to notes as well. Such a transaction is not a payment, but a promise."

To similar effect, *Boyd v. Peach Bottom R. Co.* (1879) 90 Pa. St. 169. See also *Oler v. Baltimore & Randallstown Railroad* (1874) 41 Md. 583. But cf. *Judah v. American Live Stock Ins. Co.* (1853) 4 Ind. 333; *Wight v. Shelby R. Co.* (1855) 16 B. Mon. (Ky.) 4, 63 Am. Dec. 522; *Vicksburg & C. Railroad v. McKean* (1857) 12 La. Ann. 638; *Phoenix Warehousing Co. v. Badger* (1876) 67 N. Y. 294.—Eds.

Case
supra
falls under
this head

and figures as follows: "For the purpose of organizing a corporation with a capital stock of \$15,000 to bore for gas, oil, or coal, at or near the city of Hastings, Adams county, Nebraska, and to buy or lease the land to experiment thereon for such purposes, and to buy, lease, or hire the necessary machinery and labor for such purposes, we, the undersigned, agree to subscribe and pay for the amount of stock set opposite our names; said stock to be paid for in the manner following, to-wit: Ten per cent within thirty days from the organization of said corporation, and the balance at the call of the directors; provided, that said directors shall not have power to call for more than ten per cent of said stock at any one time; and provided further, that payment shall not be called for oftener than once a month. Names, Capps & McCreary; number of shares, ten shares; dollars, \$100.00." The case was tried to the court, a jury being waived, resulting in a finding and judgment in favor of the prospecting company, and Capps and McCreary bring the case here for review.

The only errors assigned are that the finding and judgment of the court are contrary to the evidence and the law. The undisputed evidence in the case is that the plaintiffs in error and a number of other citizens signed the subscription paper quoted above; that after the \$15,000 of stock had been subscribed, the subscribers, or some of them, met and elected a board of directors, adopted articles of incorporation, and filed a copy of the same in the office of the secretary of state and the original in the office of the register of deeds of Adams county, the county in which the principal place of business was fixed by the articles of association. This incorporation, or attempted incorporation, occurred on the 15th day of April, 1889. The articles of incorporation were never filed in the office of the county clerk of Adams county. We have here then the questions: First, whether the prospecting company failed to become, as it attempted, a corporation *de jure* by neglecting to file in the office of the county clerk its articles of incorporation; second, and if it did, whether such default or failure on the part of the prospecting company is available as a defense to the plaintiffs in error? The first inquiry which presents itself is as to the nature of the agreement which the plaintiffs in error signed. What did they promise to do? We think a fair construction of the writing signed by them amounts to this: That they agreed to accept and pay for ten shares of the capital stock of the corporation the subscribers to the enterprise of boring for gas should organize, such payment to be made within thirty days after such corporation should be organized. The next inquiry is, what is meant by the expression, "when the corporation shall be organized"? It must be remembered that the plaintiffs in error agreed to become stockholders in the corporation that should be formed, and a fair construction of this promise is that they meant to become stockholders in a corporation *de jure* and not a corporation *de facto*. A *de jure* corporation is one whose right to exercise a corporate function would prove invulnerable if assailed by the state in quo warranto proceed-

ings. The plaintiffs in error might have been willing to invest a part of their capital towards a public enterprise and take their chances of the investment being remunerative, if no further liability would attach to them than that of stockholders in a *de jure* corporation, when they would not have embarked the same money for the same purpose in a partnership or a *de facto* corporation, where they would assume liabilities greater than those of stockholders in a *de jure* corporation. We hold, then, that by the subscription signed by the plaintiffs in error they promised to take and pay for ten shares of the capital stock of such *de jure* corporation as might be formed for the purpose for which the subscription was made.

Is the Hastings Prospecting Company, or has it ever been, a *de jure* corporation? It is admitted that it did not file in the office of the county clerk of Adams county, that being the county in which its articles of incorporation fixed its principal place of business, its articles of incorporation. Did this default prevent the Hastings Prospecting Company from becoming a corporation *de jure*? The authorities are not entirely in harmony on this question, but the weight of authority is, that where the statute requires the articles of incorporation to be filed with some public officer before the commencement by the proposed corporation of the business for which it is organized, such filing is a condition precedent to the right of such corporation to perform any corporate function; consequently, until a compliance with the statute, the corporation has no valid existence as a *de jure* corporation. (The learned judge proceeded to consider the authorities and concluded :) We think, therefore, that the Hastings Prospecting Company, the name of the corporation attempted to be organized by the subscribers who signed the subscription on which the plaintiffs in error are sued, is not, and has never been, a corporation *de jure*.

Is that fact available to the plaintiffs in error as a defense to this suit? It is to be borne in mind that the plaintiffs in error did not subscribe for the stock of any corporation, either *de facto* or *de jure*, then in existence; and there is a distinction as to the liability of parties for subscriptions to a corporation, or an association which assumes to be and is acting as a corporation, and the liability for subscriptions made by parties for the purpose of organizing a corporation from among the subscribers. If the subscription made by Capps & McCreary had been made to the Hastings Prospecting Company when it was acting as a corporation, when it was exercising the functions of a corporation, when it was claiming to be a corporation, and had their agreement been to pay such corporation certain sums of money for certain shares of its stock, it seems that they would then be estopped from setting up as a defense that the prospecting company was not a corporation *de jure*. (Cook, Stock & Stockholders, sec. 186, and cases cited.) Morawetz on Private Corporations, section 67, thus lays down the rule in such cases: "Every subscription (to the stock of a corporation to be organized) by implication

refers to and incorporates the terms of the charter or general law under which the corporation is to be formed; and every subscriber agrees to become associated with the others only upon condition that the formalities prescribed by the charter shall be observed in making the mutual contract. Thus, if certain preliminaries, such as the filing of a certificate, are required to be performed after the articles of association have been subscribed, but before the corporation shall be in existence, the contract of membership does not go into effect until these formalities are complied with, and a subscriber to the articles cannot until then be made to contribute the amount of his subscription." In *Rikhoff v. Brown's Rotary Shuttle Sewing Machine Co.*, 68 Ind., 388, it was held: "A subscription of stock to preliminary articles of association, not purporting to be a contract with an existing corporation, does not estop the subscriber to afterward deny the existence of the corporation in a suit upon the subscription." See, also, *Indianapolis Furnace & Mining Co. v. Herkimer*, 46 Ind., 142, where it is said: "Until the statutory requirements to organize a corporation have been complied with, a subscriber to the articles of association is not estopped to deny the existence of the corporation." (See, also, *Dorris v. Sweeney*, 60 N. Y., 463.) We think these authorities are decisive of the case under consideration. The rule they lay down is sound law, good sense, and exact justice.

If the plaintiffs in error are to pay for the stock subscribed, it of course follows that they become entitled to the stock. This would make them stockholders in a *de facto* corporation and liable as co-partners, whereas their contract was to become liable as stockholders. The plaintiffs in error have not broken their promise.

The judgment of the district court is *reversed*.⁵

⁵ *Williams v. Citizens' Enterprise Co.* (1899) 153 Ind. 496, 55 N. E. 425, *Accord. Cf. Planter's & Co. Packet Co. v. Webb* (1905) 144 Ala. 666, 39 So. 562; *Rice v. Rock Island & Co. R. Co.* (1859) 21 Ill. 93.

Rapallo, J., in *Dorris v. Sweeney* (1875) 60 N. Y. 463, at p. 467: "It may be that a corporation *de facto* was established, and that if the defendant had contracted with it after its formation he would have precluded himself from setting up the invalidity of its organization as a defence to an action upon his contract. This, however, would rest upon the ground that by contracting with it he had recognized its existence as a corporation. No such ground could be assumed where the contract was made before the formation of the corporation, and was conditioned upon its formation. A legal and effectual formation of a corporation or joint stock company for the purpose specified in the contract was a condition precedent to his obligation to put in his capital. He would not be bound under such a contract to invest his capital in the stock of a corporation not legally formed." See also *Indianapolis Furnace & Co. v. Herkimer* (1876) 46 Ind. 142.

That some subscribers were corporations, unauthorized to subscribe, will not defeat liability on a stock subscription. *McCoy v. World's Columbian Exposition* (1900) 186 Ill. 356, 57 N. E. 1043; *United States Vinegar Co. v. Foehrenbach* (1895) 148 N. Y. 58, 42 N. E. 403. As to power of a corporation to subscribe for stock or be an incorporator, see *Central R. Co. v. Pennsylvania R. Co.* (1879) 31 N. J. Eq. 475.—Eds.

ALLMAN v. HAVANA, ETC., R. CO.

1878. 88 Ill. 521.

APPEAL from the Circuit Court of Champaign county; the Hon. C. B. SMITH, Judge, presiding.

MR. JUSTICE BREESE delivered the opinion of the Court:

This was an action commenced, originally, before a justice of the peace of Champaign county, by the Havana, Rantoul and Eastern Railroad Company, plaintiffs, and against Frederick Allman, defendant, to recover an instalment or assessment of ten per cent on his subscription of five hundred dollars to the capital stock of that company. There was a judgment for the plaintiffs for fifty dollars, being the amount of the assessment. On appeal to the circuit court by the defendant, the cause was submitted without a jury, and there was a like finding, and judgment for the plaintiffs, to reverse which the defendant appeals, and insists there was no power in the corporation to make this assessment, and no liability upon him to respond to it; and further, that he had no notice of the assessment before suit brought.

Appellees claim to be a corporation, under the law of March 1, 1872, and it is necessary to determine what powers and capacities that law conferred. After providing, in section 1, that any number of persons, not less than five, may become an incorporated company, for the purpose of constructing and operating a railroad, and, by section 2, that such persons shall organize by adopting and signing articles of incorporation, which shall be recorded in the office of the recorder of deeds in each county through or into which such road is proposed to be run, and in the office of the Secretary of State, section 3 prescribes the constituents of such articles as, first, the name of the proposed corporation; second, the places from and to which it is intended to construct the road; third, the place at which shall be established and maintained the principal business office of the corporation; fourth, the time of the commencement and the period of the termination of such corporation; fifth, the amount of the capital stock; sixth, the names and places of residence of the several persons forming the association for incorporation; seventh, the names of the members of the first board of directors, and in what officers or persons the government of the proposed corporation and the management of its affairs shall be vested; and, eighth, the number and amount of shares in the capital stock of such proposed corporation. Section 4 provides, when the articles are filed and recorded, the persons named as corporators therein shall thereupon become and be deemed a body corporate, and shall thereupon be authorized to proceed to carry into effect the objects set forth in such articles, in accordance with the provisions of this act, and, as such corporation, shall have succession, and in their corporate name may sue and be sued, etc., may have a common seal, may declare the interests of its

stockholders transferable, establish by-laws and make all rules and regulations deemed necessary for the management of its affairs. Section 5 limits its duration to fifty years. Section 6 provides for recording the by-laws, as provided with respect to recording the articles of incorporation. Section 7 provides for having and maintaining a public office, where transfers of its stock shall be made, and books be kept, in which shall be recorded the amount of capital stock subscribed, and by whom, the names of the owners of the stock, the number of shares held by each person, and the number by which the shares are designated, etc., the amount of the stock paid in, and by whom, etc.

It is contended by appellant that these sections are preliminary only, and for the purpose of setting the enterprise on foot, no power existing in their charter directors to incur liabilities by which the stockholders might be involved, and refers to section 8 to sustain this view. That section provides that all the corporate powers of every such corporation shall be vested in and be exercised by a board of directors, who shall be stockholders of the corporation, and shall be elected at the annual meetings of stockholders at the public office of such corporation, within this State. The number of such directors, the manner of their election and the mode of filling vacancies, shall be specified in the by-laws, and shall not be changed except at the annual meetings of the stockholders. The first board of directors shall classify themselves, etc.

Section 13 provides that the directors of such corporation may require the subscribers to the capital stock to pay the amount by them respectively subscribed in such manner and in such instalments as they may deem proper. If any stockholder shall neglect to pay any instalment, as required by a resolution or order of such board of directors, the board shall be authorized to declare such stock, and all previous payments thereon, forfeited for the use of the corporation, but shall not declare such forfeiture until they have caused a written notice to be served on such stockholder, personally or by mail, or, if dead, to his legal representatives, stating that, in accordance with a resolution of the board, he is required to make such payment at a time and place, and in the manner to be specified in such notice, and that if he fails to make the same in the manner specified, his stock, and all previous payments thereon, will be forfeited for the use of such corporation, and thereafter such corporation, should default in payment be made, may sell the same and issue new certificates of stock therefor, provided the notice is served or deposited in the mail at least sixty days previous to the day on which such payment is required to be made.

We are inclined to think, in view of this legislation, the charter directors could do such acts only as were necessary to set the association in motion as a corporation, not to make contracts or incur liabilities for the construction of the road in which no one of them may have had a pecuniary interest as a stockholder. These were to

be left to the judgment and decision of the directors elected by the stockholders. Without expressing any definite opinion on this point, we are informed by the record that, by the articles of association filed and recorded, the capital stock of this corporation was fixed at one million of dollars, and the shares of capital stock to be ten thousand, of one hundred dollars each, and when this call was made on appellant, August 1, 1874, the sum of one hundred and fifty one thousand two hundred dollars had been subscribed.

1 The question is, and it is the important question in the case, was it in the power of these directors to make this call, the full amount of the capital stock not having been subscribed? This question is to be decided by authority. On reference to a leading work on railways, 1 Redfield on the Law of Railways, 176, we find it is there said, that it is an essential condition to making calls in these companies, where the number of shares and the amount of capital is fixed, that the whole stock shall be subscribed before any call can lawfully be made. Reference is made in support of the text to *Stoneham Branch R. R. Co. v. Gould*, 2 Gray, 277, in which CH. J. SHAW uses this emphatic language: It is a rule of law too well settled to be now questioned, that when the capital stock and the number of shares are fixed by the act of incorporation (in this case by the articles filed and recorded), or by any vote or by-law passed conformably to the act of incorporation, no assessment can be lawfully made on the share of any subscriber until the whole number of shares has been taken. This was held in *Salem Mill-dam v. Roper*, 6 Pick. 23, and 9 Pick. 187; *Cabut and West Springfield Bridge v. Chapin*, 6 Cush. 50; *Worcester and Nashua R. R. Co. v. Hinds*, 9 Cush. 110.

The chief justice says this is no arbitrary rule—it is founded on a plain dictate of justice and the strict principles regulating the obligation of contracts. When a man subscribes a share to a stock to consist of one thousand shares, in order to carry on some designated enterprise, he binds himself to pay a thousandth part of the cost of such enterprise. If only five hundred are subscribed for, and he can have no assurance, which he is bound to accept, that the remainder will be taken, he should be held, if liable to assessment, to pay a five hundredth part of the cost of the enterprise, besides incurring the risk of an entire failure of the enterprise itself, and the loss of the amount advanced toward it. The same doctrine is held in *Somerset and Kennebec R. R. Co. v. Cushing*, 45 Me. 124. Other cases might be cited, but it is unnecessary.

By the articles of incorporation filed and recorded a corporation was created, as efficient for all the contemplated purposes as if its power had been conferred by a special charter. The capital stock was fixed, definitely, at one million of dollars, to be divided into ten thousand shares, of one hundred dollars each, and that amount must have been subscribed before the corporation could have a legal existence. It was a condition precedent to the legal existence of the

company. There is nothing in the "articles" or in the statute which authorizes the corporation to commence operations when a less amount is subscribed.

Very many charters might be cited which declare, when a less amount than the whole capital stock is subscribed the corporation may proceed in their business; but nothing of that sort is found in this case.

There are various other points and objections made by appellant which need not be noticed, as what we have said "cuts the case up by the roots," and there can be no recovery.

The judgment of the circuit court is reversed.

*Judgment reversed.**

HUGHES v. ANTIETAM MFG. CO.

1870. 34 Md. 316.⁷

APPEAL from the Circuit Court for Washington County. The facts are sufficiently stated in the opinion of the Court.

ROBINSON, J., delivered the opinion of the Court.

This is an action of assumpsit by the appellee, claiming to have been incorporated in pursuance of the 40th section of Article 26, of the Code of Public General Laws, to recover certain unpaid instalments, alleged to be due on the subscription of the appellant to its capital stock.

The following is a copy of the recorded certificate, to which the subscription is affixed: "The undersigned, free white citizens of the State of Maryland, desiring to form a company for the purpose of manufacturing, under the name and style of the Antietam Manufacturing Company of Washington County have fixed the capital stock of said company at \$150,000; said capital stock shall consist of five hundred shares, at \$100 per share, the term of existence of said company or corporation not to exceed the term of forty years. The

* *Accord*, *Memphis Branch R. Co. v. Sullivan* (1876) 57 Ga. 240; *Temple v. Lemon* (1884) 112 Ill. 51; *Oldtown &c. R. Co. v. Veazie* (1855) 39 Maine 571 ("The subscription having been made before the corporation was organized, was necessarily as well as in terms subject to a condition, that the party to accept it should have a legal existence, and should obtain the capital required by its charter and referred to in the subscription, by which it became a part of it"); *Bray v. Farwell* (1880) 81 N. Y. 600; *Myers v. Sturgis* (1908) 123 App. Div. (N. Y.) 470, 108 N. Y. S. 528, *affd. short*, (1910) 197 N. Y. 526, 90 N. E. 1126.

Contra, *Schenectady &c. Plank Road Co. v. Thatcher* (1854) 11 N. Y. 102, *semble*.

See *Salem Mill Dam Corporation v. Ropes* (1827) 6 Pick. (Mass.) 23; *Bucksport &c. R. Co. v. Buck* (1876) 65 Maine 536.

As to the effect and operation of statutory provisions, see *Lincoln Shoe Mfg. Co. v. Sheldon* (1895) 44 Neb. 279, 62 N. W. 480.—Eds.

⁷ Statement abridged. Portion of opinion omitted.—Eds.

company shall be managed by a president and ten directors for the first year. In testimony whereof we have each subscribed for the number of shares set opposite our names." To which is affixed the subscription of the appellant, for fifty shares, five thousand dollars. * * *

But conceding the validity of the subscription, it is contended that an action of assumpsit will not lie, because it does not contain an express promise to pay, and that the only remedy against the delinquent subscriber is by a forfeiture and sale of the stock under the 45th section. It may be true, that an express promise in so many words, may not be found in the subscription, but it was made for a given number of shares and at a fixed money value, and when construed in connection with the law under which the company was to be organized, we are very far from admitting it does not amount to an express promise to pay for the shares in the manner and upon the conditions therein prescribed. The purpose of the appellant and his co-subscribers in signing the articles of association and subscribing for a given number of shares, was to organize a company and furnish capital sufficient to carry on the manufacturing business, from the successful prosecution of which they expect to realize a profit on the money thus invested. To this end property was to be purchased, materials bought, labor performed, and debts incurred, and these could only be done and accomplished by the payment of the stock subscribed. Forfeiture and sale of the shares might fail to realize the means necessary to effect these objects, and particularly if the prospects of success were not so flattering after the organization as the more hopeful projectors anticipated. If, therefore, no action will lie to enforce the payment of the subscriptions, not only must the object and purposes for which the company was organized fail, but the capital stock of those who have promptly paid, relying upon the good faith of their co-subscribers, must also prove an entire loss. It has been held, it is true, in Massachusetts and New Hampshire, that the only remedy against the delinquent subscriber is by forfeiture and sale of the stock; but in reviewing these decisions, Mr. Redfield says, "they arose under charters in which the capital stock and number of shares were not fixed, and he admits it to be firmly established in this country and in England that where the stock of the company is defined and divided into a certain number of shares, a subscription for shares whether it contains an express promise to pay or not, is regarded as an agreement on the part of the subscriber to pay for the same according to the terms and provisions of the charter, and that the remedy by forfeiture and sale is cumulative merely." 1 Redfield on Railways, 163. The many cases referred to by the author fully sustain this general rule, and in one of them, the Hartford and New Haven R. R. Co. vs. Kennedy, 12 Conn., 500, where the decisions in Massachusetts relied on by the appellant were ably reviewed, the Court say: "The act of becoming a stockholder pursuant to the provisions of this

charter, is one from which the law raises a promise to pay the instalments legally assessed and demandable. The common law furnishes a remedy for a violation of this engagement by an action of *assumpsit*. The subsequent enactment authorizing the directors to sell the stock is affirmative in its terms. It does not expressly or by implication take away the previous remedy which the common law has provided. No words are used indicative of an intention to deprive the corporation of their previous existing remedy—no necessity is perceived why they should be deprived of it—and every consideration arising from public policy or connected with good faith and common honesty demands that this remedy should continue in full force.”

But it is further insisted, that the appellant had the right to withdraw his subscription after the acknowledgment of the certificate before the justice of the peace, and at any time prior to its being recorded. We think, however, it is clear, both upon principle and authority, he cannot. As we have before said the subscription is in itself a contract on the part of the appellant to pay for the shares thus taken in the manner and according to the terms prescribed by law, in consideration of which he acquired the right to demand the same upon the organization of the company, and of which he could not be deprived, either before or subsequent to the incorporation. The obligation to pay on the one hand, and the right to demand on the other, created a mutuality of contract, binding as between the co-subscribers, the parties thereto, and could not be discharged by the act of one, without the assent of the other. And this too seems to be well settled. In *Angell & Ames on Corporations*, sec. 523, the rule is thus stated: “A person subscribing before the organization of a proposed incorporated joint stock company, raises a mutuality in his contract which will render him liable to the company after incorporation. A subscriber or partner in an intended undertaking, subscribing an agreement to take measures to carry out the same, cannot discharge himself of liability or repudiate the concern to which he may have thus pledged himself; and if an Act of the Legislature has been passed for effectuating the purpose of the undertaking, by which certain obligations are created, such an original subscriber is not exonerated from the liabilities imposed by the Act, by having, during the progress of the bill, renounced all further connection with the undertaking, and desired that his name might be in consequence omitted from the Act.”

In *Kidwelly Canal Co. v. Raby*, 2 Price, 93, 1 Ex., where this question came directly before the Court, Richards, B., said: “If Raby had not endeavored to withdraw, there could have been no doubt of his liability; then the question becomes, whether he has in fact withdrawn; and I think he has not, inasmuch as he could not do so without the consent of all those with whom he had become engaged in the undertaking.” The subscription in this case was made in contemplation of a charter by the Legislature, but in Lake

Ontario, &c. R. R. Co. v. Mason, 16 N. Y., 463, the rule thus laid down was recognized and extended to a subscription to articles of association, signed with a view of being incorporated under a general law, and Selden, J., said: "If the contract to pay for and take the stock was a valid contract, made upon a sufficient consideration, then subscription was not open to revocation until the incorporation of the company was perfected, the other subscribers had an interest in its execution and performance, of which they could not be deprived by the act of the defendant."

We find no error in the rejection of the appellant's third prayer. In order to avoid the contract of subscription, it must appear to have been made upon the faith of false representations of the agent, in regard to a matter of fact, material to the value and success of the enterprise. The mere statement that the rents of the Emmert property would pay six per cent on the capital stock for the first year, and then the company could determine whether to build or not, &c., must be regarded as the mere expression of opinion in regard to the success of the undertaking, upon which the appellant had no right to rely. In all probability, he was as competent to judge of the success, or profits to be realized as the agent, and contracts thus deliberately made, and upon the faith of which others may have acted, are not to be avoided, because of the flattering prospects held out by parties soliciting subscriptions.

The appellant's eighth prayer was also properly rejected. This was a joint undertaking, and the consideration of the contract of subscription was the right to share the profits arising therefrom. Under such circumstances, a subscriber could neither withdraw nor be released from his subscription without the consent of all the co-subscribers, and the fact that the directors or managers undertook to release certain parties, cannot operate in any manner to discharge the appellant from his obligation.

The statute under which the appellee was organized, confers no such power on the directory, and the exercise of it cannot affect, one way or the other, the liability of the subscribers who may have been thus released.

We think, however, the Court erred in the modification of the appellant's second prayer. The change of the capital stock from fifty to one hundred and fifty thousand dollars, after his subscription, and without his assent or subsequent acquiescence, discharged him from all liability on account of the same, and the mere acknowledgment by him of the certificate before the justice of the peace, if, at the time, he was ignorant of the change or alteration thus made, cannot be construed as a new contract on his part, nor estop him from relying on this defence in a suit by the appellee—the party by whom the change was made.

We think, also, the Court erred in regard to the notice prescribed by section 49 of Article 26. It has been decided, we are aware, in one or two States, under statutes similar in many respects to the

one under which the appellee was organized, that notice of the calls or assessments is only necessary to the forfeiture and sale of the stock; but in referring to these cases, Redfield says: "They are contrary to the general course of decisions upon the point, and somewhat at variance with the idea of a call or assessment." 1 Redfield on Railways, 147, note. To say that it is unnecessary, because the subscribers, who may be living in different parts of the county, and perhaps the State, are presumed in law to know all that is done by the directory, seems to us to be raising a presumption against the truth itself. But apart from these views, we think the 49th section, in express terms, provides, that notice shall be given. It says the directors, trustees or managers "may call in and demand from the stockholders respectively, all sums of money by them subscribed, at such times," &c. How demand? It certainly was not the intention of the Legislature that it should be made for the first time through a suit, without giving the subscriber an opportunity to pay the instalment thus assessed. Nor was such a construction put upon the statute by the appellee, for we find that written notice was mailed to the appellant. The 49th section, however, requires that there should be a "personal demand," or "notice published, nearest to the place where the business of the corporation shall be carried on." Constructive notice by the mail is not a personal notice, although in some cases by express statutory provision it is sufficient to bind parties. Here, however, the manner of giving notice is prescribed by the law under which the calls are made, and it was the plain duty of the directors to have complied strictly with its requirements in this respect. They had no right to dispense with the mode and manner of notice thus prescribed, and where, by positive law, personal notice is required, a written notice through the mail is not a compliance with the statute.

There is another objection, which, so far as the record discloses, is fatal to the right of the appellee to recover in this suit. The capital stock of the company, and the number of shares, and their par value per share, are fixed in the recorded certificate, and there is no provision either in the articles of association, or the subscription itself, or the general law under which the appellee was organized, authorizing the directors to make calls or assessments before the whole capital stock is taken. We take the general rule to be, that where the capital stock and the number of shares are fixed in the articles of association or recorded certificate, no valid assessments or calls can be made against a subscriber until all the shares are taken, unless there be a provision to that effect either in the certificate or general law under which the company is organized, and for the reason that the success of the enterprise, and the profits to be realized therefrom, may depend entirely upon having the full amount of the capital taken up. Cabot and West Springfield Bridge Co. v. Chapin, et al., 6 Cushing, 50; Contoocook Valley Railroad v. Barker, 32 N. H. 370; Fox v. Clifton, 6 Bing., 776; Wentner v.

Shairp, 4 Man. Grang. & Scott, 404; Pitchford v. Davis, 5 Meeson & Welsby, 2; Norwich & Lowestoft Comp. v. Theobald, 1 Moo. & Mal., 151, and 1 Red., 176. The author says: "And where the charter of a railway company requires their stock to consist of not less than a given number of shares, assessments cannot be made before the required number is taken." This point was not relied on in the argument, and we do not rest our decision upon it, for although the record shows only about one-third of the stock was taken, it may appear by proof not before us, that the whole capital stock was subscribed.

Being of opinion that the Court erred in the modification of the appellant's second prayer, and also in granting the appellee's first prayer, so far as regards the notice of the assessments or calls, the judgment will be reversed, and a new trial awarded.

*Judgment reversed, and new trial awarded.**

FORT EDWARD ETC. PLANK ROAD CO. v. PAYNE.

1857. 15 N. Y. 583.

APPEAL from the Supreme Court. The action was tried before a referee, who found the following facts:

The plaintiff was duly incorporated under the act of May 7th, 1847, providing for the incorporation of turnpike and plank road companies, its articles of association having been filed January 13th, 1850. The sixth section of the articles is as follows: "For the purpose contemplated by these articles, the undersigned have severally subscribed for the number of shares of the capital stock of this association placed opposite their respective signatures hereto, and they severally agree, to and with each other, to pay to the said Fort Edward and Fort Miller Plank Road Company their respective sub-

* That subscriptions in an incorporation paper are not revocable, see *accord*, Pacific Fruit Co. v. Coon (1895) 107 Cal. 42, 40 Pac. 542.

PAYMENT FOR SHARES.—An agreement to take stock implies an agreement to pay for it. San Joaquin Land & Water Co. v. Beecher (1894) 101 Cal. 70, 35 Pac. 349; Crawford v. Roney (1906) 126 Ga. 763, 55 S. E. 499; Wood Harvester Co. v. Robbins (1893) 56 Minn. 48, 57 N. W. 317; Buffalo &c. R. Co. v. Dudley (1856) 14 N. Y. 336; Windsor Elec. Light Co. v. Tandy (1893) 66 Vt. 248, 29 Atl. 448, 44 Am. St. 838. As said by Haralson, J., in Planter's &c. Packet Co. v. Webb (1905) 144 Ala. 666, 39 So. 562, "That a subscription for stock implies a promise to pay for it, even though the subscription was before incorporation is the rule sustained by the great weight of authority."

In some New England states, a different rule is prevalent and proof of an express promise to pay is requisite. See Andover &c. Turnpike Co. v. Gould (1809) 6 Mass. 40, 4 Am. Dec. 80; Mechanic's &c. Machine Co. v. Hall (1876) 121 Mass. 272; Kennebec &c. R. Co. v. Kendall (1850) 31 Maine 470; Belfast &c. R. Co. v. Moore (1872) 60 Maine 561; New Hamp. Central R. v. Johnson (1855) 30 N. H. 390, 64 Am. Dec. 300.

RELEASE AND DISCHARGE.—In Cartwright v. Dickinson (1889) 88 Tenn. 476,

scriptions for said capital stock, whenever called for by said directors or their successors in office." The defendant did not subscribe the articles; but he, with others, subscribed an instrument in writing, dated March 1, 1850, which, after reciting that at a meeting of the directors of the company, held February 19th, 1850, it was resolved that the directors adopt and establish, as the terminus of their road, some convenient point at or near Saratoga bridge, commonly called Fort Miller bridge, in the town of Greenwich, and that the directors construct or cause to be constructed the whole of their road, extending from Fort Edward village to the said bridge, the present year, proceeded as follows: "Now we, the undersigned, subscribe for the number of shares to the Fort Edward and Fort Miller Plank Road Company set opposite our respective names, upon condition that the road is extended to Fort Miller bridge, so as to make that its southern termination." This instrument is written in a book of the company, following the record of its articles of association.

The road which the company was organized to construct, as appears from the articles of association, was to extend from the village of Fort Edward to the village of Fort Miller, a distance of about eight miles, with the privilege of extending it to a point near Saratoga bridge, about two and one-half miles further.

The action was to recover the amount of the defendant's subscription, the directors having made the calls for the payment of the whole amount of subscriptions to stock, and given the requisite notices thereof, pursuant to the act.

The referee reported that the plaintiff was entitled to recover the amount of the defendant's subscription. The judgment rendered on his report having been affirmed by the Supreme Court, at general term in the fourth district, the defendant appealed to this court.

BOWEN, J.—I think that the instrument signed by the defendant is wholly void, by reason of the condition therein contained. It was intended as a subscription to the capital stock of the company. The act under which the plaintiff was incorporated prescribes the manner of subscribing for stock, and only authorizes absolute sub-

12 S. W. 1030, 7 L. R. A. 706, 17 Am. St. 910, *held* that no power resides in a corporation, its officers or directors, to release a shareholder from payment of his stock subscription, but this can be effected only upon the unanimous consent of the shareholders, "rights of creditors being out of the way." Lurton, J., said: "The contract of share-holders is a mutual one. Without the consent of all one cannot be released from liability. Even a board of directors cannot discharge the contract of a share-holder to pay for his shares according to his contract, or disfranchise him by a forfeiture declared without express authority of law" (p. 483). See also *Memphis Branch R. Co. v. Sullivan* (1876) 57 Ga. 240; *Bouton v. Dement* (1888) 123 Ill. 142, 14 N. E. 62; *McNulta v. Corn Belt Bank* (1897) 164 Ill. 427, 45 N. E. 954, 56 Am. St. 187; *Bedford R. Co. v. Bowser* (1864) 48 Pa. St. 29.

A subscriber may be released, however, as part of a compromise made in good faith. *New Albany v. Burke* (1870) 11 Wall. (U. S.) 96, 20 L. ed. 155.—
Eds.

scriptions. This case cannot be distinguished in principle from *Butterworth, etc., Turnpike Company v. North* (1 Hill, 518). It was held, in that case, [that to allow subscriptions to the stock of such a corporation to be received, conditioned that a particular location of the proposed road should be adopted, would be contrary to public policy, as by such means improper influences might be brought to bear upon the question of the location.] The object had in view by the legislature, in authorizing the formation of these corporations, was to benefit the public generally, by providing for the construction of safe and commodious highways, so located as to be most convenient and beneficial. If the interest of the stockholders, in such a company, is allowed to control the question, such a location and such termini of the proposed road will almost invariably be adopted as will best subserve the public interest; when if, in order to procure the requisite amount of capital, subscriptions are allowed to be taken, conditioned that a particular location or terminus be adopted, public convenience will frequently be sacrificed to individual interest.

By the articles of association of this company, their road was to be constructed from Fort Edward to Fort Miller, a distance of eight miles, with the privilege of extending it to Saratoga bridge, two and one-half miles further; and a large majority of the stockholders became such by subscribing the articles, which left it optional with the directors whether the road should be extended. These stockholders had the right not only to expect, but to require, that it should not be extended unless the interest of the company would be thereby promoted; but by receiving these conditional subscriptions the directors were obliged to extend the road, although every dollar expended for that purpose will be a total loss to the corporation, and none be benefited thereby except those at whose instance it was done.

The judgment appealed from should be reversed and a new trial granted.

DENIO, C. J., SELDEN, SHANKLAND and PAIGE, Js., concurred; JOHNSON, J., expressed no opinion; COMSTOCK and BROWN, Js., not having heard the argument, took no part in the decision.

*Judgment reversed and new trial ordered.**

CALEY v. PHILADELPHIA ETC. R. CO.

1876. 80 Pa. St. 363.

THIS was an action of assumpsit brought June 4th, 1873, by The Philadelphia and Chester County Railroad Company against David

* *Butternuts &c. Turnpike Co. v. North* (1841) 1 Hill (N. Y.) 518; *Craig v. Andes* (1883) 93 N. Y. 405, esp. 414, *Accord*. See also *Pittsburgh &c. R. Co. v. Stewart* (1861) 41 Pa. St. 54, 58 (subscription prior to organization

P. Caley. The action was to recover an instalment of \$5 per share on ten shares of the stock of the plaintiffs.

By the Act of March 17th, 1871 (Pamph. L. of 1872, p. 1269), commissioners were appointed to open books and receive subscriptions for the plaintiffs' company, by the name of The Philadelphia, Delaware and Chester Central Railroad Company, subject to the provisions of the General Railroad Law of February 19th, 1849; the capital stock to be \$500,000 and to be divided into shares of \$50 each, with authority from time to time to increase the capital so much as the company might think necessary to complete the road. The road was to commence "at or near Philadelphia" and terminate at some point on the Pennsylvania Railroad, east of Dowingtown, in Chester County. Letters patent were issued to the company on the 13th of October, 1871.

Afterwards the company opened a subscription for stock under which, amongst others, the defendant subscribed for ten shares.

The subscription was as follows:

"We, the undersigned, subscribers for the number of shares in the capital stock of the Philadelphia, Delaware and Chester Central Railroad Company, set opposite our names respectively, and agree to pay for the same as the directors of said company may call for instalments, in accordance with the provisions of the law regulating the collection of instalments on subscriptions to the capital stock of railroads. The route of the proposed railroad to be as follows: Commencing at a point on the Pennsylvania Railroad at or near Hestonville, thence by the most practicable route to the valley of Cobb's creek, * * * then along Fawkes' and Caley's runs to Newton Square; thence, via Sugartown and Goshenville by the most expedient route to be surveyed to West Chester, and from thence to Dowingtown, as soon as sufficient funds shall be subscribed to carry on the work."

Afterwards by Act of April 9th, 1872 (Pamph. L. of 1873, p. 1084), the name of the company was changed to "The Philadelphia and Chester County Railroad Company."

The case was tried February 25th, 1875, before Clayton, P. J.

The plaintiffs gave in evidence the Acts of Assembly, grant of letters patent and the subscription. They also proved the call for instalments, &c.

Tryon Lewis, the president of the company, testified: that the road had been commenced on September 11th, 1872, about three-quarters of a mile east of Newtown Square.

On cross-examination he said; that they could not say that the route had been permanently fixed east of Darby creek; the route would be subject to improvement; the following resolution was the last act of the board of directors in reference to the location of the road: "That the eastern terminus of the line be fixed on the

must be unconditional, distinguishing subscription after organization has been effected); *Bucksport &c. R. Co. v. Buck* (1878) 68 Maine 81.—Eds.

West Chester and Philadelphia Railroad at or near Christian Street," &c.; the terminus in the resolution was four or five miles from the terminus at Hestonville, provided for in the subscription, but in the landing in the city, the final terminus would be about one square distant; one being on Market street and the other on Chestnut street. The amount of subscriptions was \$84,500; no work had been done on the line outside of that prescribed in the subscription-book; he could not say that any terminus had been settled at all. Caley's subscription was after granting the letters patent.

The defendant offered to prove as follows:—

1. That at the time he made his subscription the route of the road was staked out through his lands, and that as an inducement for him to subscribe, the president or other officers of the company assured him, if he would subscribe, that the road should be built upon that route through his lands.

2. That he asked the directors of the company, or some of them, what guaranty he would have that the road would be built, to which they replied, that the road would not be undertaken nor his subscription called for, till \$150,000 or \$160,000 at least, of bona fide subscriptions to stock had been taken, and that this amount was fixed by them, as being in their judgment sufficient to carry on the work.

3. That the defendant subscribed upon the express condition and understanding with the officers of the company that the eastern terminus of the road should be made at or near Hestonville; that the termination of the road at this point was the main consideration for the defendant's subscription, and that he would not have subscribed to a road upon any other route.

And further, that these representations were made at a public meeting called by the company, at which were present the president, who occupied the chair, the treasurer and one or more directors.

The offer was objected to by the plaintiff, overruled by the court and a bill of exceptions sealed.

MR. JUSTICE GORDON delivered the opinion of the court, January 31st, 1876.

Where one subscribes to the stock of a public corporation prior to the procurement of its charter, such subscription is to be regarded as absolute and unqualified, and any condition attached thereto is void: *Bedford Railroad Co. v. Bowser*, 12 Wright 29. The reason for this rule is obvious; the commissioners, who are appointed to receive such subscriptions, are not the accredited agents of the corporation, for it is not yet in being, but are rather the agents of the public, acting under limited and definite powers, which every one is bound to know, and if he be misled by representations which such agents have no right to make, it is his own folly. Any other rule would lead to the procurement from the Commonwealth of valuable charters without any absolute capital for their support, and thus give rise to a system of speculation and fraud which would be

intolerable. When, however, the company is once organized, a different order prevails. Such a company may receive conditional subscriptions for its stock, and, when it does so do, it is bound to the performance of the conditions therein contained; *Railroad Co. v. Stewart*, 5 Wright 54; *Railroad Co. v. Hickman*, 4 Casey 318. Doubtless the act of incorporation might alter this rule and put all stock subscriptions within the same category, and subject them to the same conditions as those made before organization. But the Act of 1849, subject to the provisions of which the plaintiff company was erected, has in it nothing to indicate that the legislature intended to restrict the powers which corporations ordinarily possess over their own stock. It follows, that the plaintiff might dispose of its stock, as of any other of its property, in such manner as, in its judgment, might best subserve the purposes of its erection, and, to this end, might receive conditional subscriptions for such stock.

Again, after the organization of a company, chartered for some public purpose, as, in this case, for the building of a railroad, if one subscribe, without condition to the stock of such company, he does so in view of the general powers conferred upon it by the legislature, and he is responsible with his fellow corporators for the proper and lawful exercise of those powers, and he cannot, therefore, set up an unlawful act of the directors as an excuse for the non-payment of his subscription; for it is within his own power to prevent such abuse of authority.

As was said in *Graff v. The Railroad Co.*, 7 Casey 489, the contract of subscription is not only with the company, but, also, with all the other shareholders; hence the subscriber may not set up even the fraud of the directors in order to defeat his contract. But when ever a power intervenes, over which he can have no control, to alter in a material point the character of his contract without his assent, actual or implied, such intervention works his release. As, where, by Act of the General Assembly, a turnpike company was authorized to alter the termini of its road; in that case it was held that a subscriber to its stock was released from his contract of subscription: *Turnpike Co. v. Phillips*, 2 Penna. R. 184; *Plankroad Co. v. Arndt*, 7 Casey 317. The reason for this is, that such termini form part of the conditions which enter into the contract, and as the supreme power, over which the subscriber has no control, intervenes to alter such conditions, he is thereby released. A contrary doctrine would involve the unreasonable supposition that a contract might be imposed upon a party who never assented thereto.

We now come to the application of these principles to the case in hand. It is conceded that this company was fully organized at the time the subscription in controversy was made. (The learned judge here referred to the terms of the subscription contract.) By this the company undoubtedly agreed that the road shall begin and

terminate in certain points therein set forth, and that it shall, when built, occupy the route indicated.

These matters form part of the contract: *Plankroad Co. v. Arndt*, supra; and if the company has determined to abandon either of the termini or any material part of the route, as set forth in the contract, the defendant is, thereby, released from his obligation. Of this the minutes of the company were evidence; hence the second and fourth points of the defendant should have been affirmed. If the above stated doctrine be not correct, then has the defendant no remedy; for as the directors, in changing the route of their road, are acting within the powers conferred by the charter, he cannot prevent such change, though violative of the terms of the contract.

* * * * *

*The judgment is reversed, and a venire facias de novo awarded.*¹⁰

SAWYER, J., in *WHITE MOUNTAINS R. CO. v. EASTMAN*.

1856. 34 N. H. 124, 139-143.

To give the writing any validity, then, if there were no objections to it on other grounds, it would be necessary to prove that it was authorized by the directors, and that in executing it the clerk was acting as their agent, by their order. His testimony to the point, introduced by the defendant, and objected to by the plaintiffs, was, therefore, competent. The evidence shows an agreement in writing, made with the defendant's intestate, by the authorized agents of the corporation in its behalf, at the same time the subscription was made by the intestate for the thirty shares, and in reference to that subscription, and therefore binding on the corporation, unless invalid on other grounds. The two contemporaneous writings upon the same subject, between the same parties, are to be considered together as one contract, unless upon other grounds the writing given by the corporation is to be held void. Thus considered in connection, effect would be given to all the stipulations on both sides, contained in both writings, as constituting together one agree-

¹⁰ *Pittsburgh &c. R. Co. v. Biggar* (1859) 34 Pa. St. 455; *Bedford R. Co. v. Bowser* (1864) 48 Pa. St. 29; *Boyd v. Peach Bottom R. Co.* (1879) 90 Pa. St. 169, *Accord*. In the last cited case, Mr. Justice Sterrett said: "The conditional feature of the subscription furnished no ground of defence. It is scarcely necessary to repeat what has been so often said, that a subscription to the stock of a public corporation, made before letters patent are issued and an organization effected, must be considered absolute and unqualified, and any condition attached thereto void. Commissioners have no authority to receive conditional subscriptions. If they do, the subscription itself is valid and binding, and the condition null and void: *Caley v. The Railroad Co.*, 30 P. F. Smith 367" (p. 172).

See *Burke v. Smith* (1872) 16 Wall. (U. S.) 390.—Eds.

ment. If no person were to be affected by the contract but the parties themselves, it would be competent for them to agree that the intestate should take and pay for thirty shares, subject, however, to the condition, that if within one year he should elect to reduce the number so subscribed for to five, or any other number not less than five, he might be at liberty so to do, and that the corporation, upon his paying for the thirty or other reduced number of shares, would give him proper certificate therefor, constituting him the owner of them. It would be immaterial whether the whole contract appeared upon one paper, or whether one paper signed by him, promising to take and pay for thirty shares, was placed in the hands of directors as containing all the evidence necessary for them to hold to enforce their claim under the contract against him; and another paper signed by the directors, or by the clerk by their order, binding them to release him from his obligation to take and pay for so many of the shares as he had the right to repudiate, were placed in his hands as containing all the terms of the contract necessary for him to prove, if he elected to reduce the number. In either case the agreement would be the same. But while the two writings are thus considered as parts of the same agreement, when they are of a character to affect only the parties to it, they may be regarded as separate and independent contracts whenever it is necessary so to regard them in order to protect innocent third persons, having an interest in the subject matter of the agreement, from the consequences of a fraud attempted to be practiced upon them by means of it. If necessary for that purpose, the writing by which the intestate promised to take and pay for the thirty shares, may be held as between the parties themselves to be their contract, binding in law, while the other part of the agreement, evidenced by the writing held by him, may be adjudged void, as a fraud upon third persons. Of this, neither of the parties to the fraudulent agreement would have any right to complain. If they, for the purpose of misleading and deceiving third persons, having an interest in the subject of their contract, held out the subscription of the intestate, as shown upon their subscription book, as the contract between them and him, and concealed from those third persons the fact, material for them to know, that there was a secret stipulation, making the contract an entirely different thing, the principles of common honesty would require that they should be compelled to stand to the agreement, as they held it out to be. This is to be done, not for the sake of either of the parties to the fraud, but of the innocent third persons who would be wronged by giving effect to the secret stipulation, and still more deeply wronged by holding the defendants wholly exonerated from the contract. The fraud in this case consists, not in the fact that the parties agreed that the intestate should have the right to repudiate his subscription to a certain extent, but in suppressing that material feature in the agreement, and in holding out to others as their contract one which speaks in very

different terms from that which in fact they made. If the conditional character of the subscription had appeared upon the subscription book itself, by inserting the provision that the intestate was at liberty thus to reduce his subscription, no person could have been deceived, and the contract would undoubtedly have been valid. The parties, for the purposes of deception, severed and disconnected the conditional stipulation from the contract, so as to render it on its face an absolute engagement by the intestate to pay for the thirty shares, and in this form held it out to others as their true contract. In this they acted fraudulently, and neither has reason to complain if the law holds the contract as between them to be what they held it out to be to others. This is not a case for the application of the maxim that both parties, being in *pari delicto* are to be left where they have placed themselves, neither being permitted to found a claim upon their fraudulent contract against the other. The contract here set up is that by which the intestate promised to pay for the thirty shares. That was not an illegal or fraudulent contract. The fraud consisted in presenting it to others as the true contract, and the whole contract on the subject, when another secret stipulation existed, which, if permitted to stand as binding, would give full effect to the fraud. It is the secret stipulation alone which operates in fraud of others, and upon that the law leaves the parties where they stand; declining to enforce it for the benefit of either; while, as to the other part of the contract, to enforce it between the parties is what is necessary to defeat their fraudulent purpose as to other innocent persons. That the proceeding is a fraud upon third persons is clear from the relation in which subscribers for stock in a corporation of this kind stand toward each other. In the subscription of each person, every other subscriber has a direct interest. Their respective subscriptions are contributions or advancements for a common object. The action of each in his subscription to be based upon the ground that the others are what upon their face they purport to be.

The fact that one man has bound himself to place a certain amount of his money upon the risk involved in the enterprise, is an inducement to others to venture in like manner. Seeing who are his associates, and the extent of the liability which they have assumed, he regulates his own upon that consideration; and though in form and legal effect the contract of each is with the corporation, yet among the subscribers themselves it is to be regarded as an agreement with every other subscriber to bear that proportion of the common burthen to which he professes to bind himself by the contract which he holds out to them as his contract with the corporation. To hold that the secret stipulation is valid as between these parties, would be to give full effect to the fraud, by relieving the estate of the intestate from a part of that burthen which he held out to the other subscribers he had assumed, and throwing upon them the necessity of providing for it. To hold that by the fraud the whole contract

as between the parties is void, would but increase the injustice as to the other subscribers, for it would throw upon them the whole of that proportion of the common burthen which the intestate held out to them he had assumed; while, on the other hand, by holding that the contract which the parties held out to them as the true one was in fact the contract made by them—all secret stipulations rendering it other than that being void as fraudulent towards third persons—the contemplated fraud is defeated and perfect justice done to the other subscribers, and at the same time, in so holding, no wrong is done to the parties, of which either has reason to complain. The books abound with cases in which the principle is applied (that a secret agreement between the parties to a contract, changing its character from what it ostensibly is, to the prejudice of others collaterally interested, is a fraud on them, and therefore void, even as between the parties themselves.) *Jackson v. Duchaire*, 3 T. R. 551; *Wayburd v. Stanton*, 4 Esp. 179. * * *

All such private agreements are held void on the ground that good faith to the other creditors requires that the equality for which it is to be understood on the face of the composition deed they bargained among themselves, shall be preserved, and the tacit understanding that all should share alike, be fairly carried out.¹¹

WEBB v. BALTIMORE ETC. R. CO.

1893. 77 Md. 92.

APPEAL from the Circuit Court for Dorchester County. The case is stated in the opinion of the Court.

ALVEY, C. J., delivered the opinion of the Court.

This action was brought to recover of the defendant for certain stock subscribed in the plaintiff company. The declaration contains several of the common indebitatus counts, but the fifth count

¹¹ "All subscriptions are presumably upon the same basis, and all shares entitled to the same benefits and subject to the same burdens. In the subscription of each person every other subscriber has a direct interest.

There purported here to have been a large amount of stock taken, whereas, in fact, there was really no stock taken—the issue of the shares to Cushman and Hardin being coupled with the right on their part to surrender them and take back their money. Such a private arrangement with an individual subscriber, although it may not be intended, is, in law, a fraud upon the other subscribers; and such agreement will be disregarded, and the party be held bound to all the responsibilities of a *bona fide* subscriber. This is the doctrine, as we regard, abundantly established by judicial decisions." *Melvin v. Lamar Ins. Co.* (1875) 80 Ill. 446, 456-7, 22 Am. Rep. 199. *Accord*, *Galena &c. R. Co. v. Ennor* (1886) 116 Ill. 55, 4 N. E. 762; *Stone v. Vandalia &c. Coke Co.* (1895) 59 Ill. App. 536; *Minneapolis Threshing Machine Co. v. Davis* (1889) 40 Minn. 110, 41 N. W. 1026, 3 L. R. A. 796, 12 Am. St. 701 ("The familiar principle of equitable estoppel by conduct applies"); Phila-

is special, and it alleges that the defendant subscribed for and agreed to take twenty shares of the capital stock of the plaintiff company, and to pay \$1,000 therefor, on the completion of the railroad of the company to the town of Vienna, Maryland; and that, although the said railroad has long since been completed to the said town of Vienna, and that the said subscription is due and demandable, the defendant has not paid the same, or any part thereof. By the pleas, the defendant denied the legal existence of the contract alleged, or that he was in any manner bound thereby.

The questions presented on this appeal are simply as to the admissibility of evidence, and are presented by two bills of exception taken by the defendant.

At the trial it was admitted that the plaintiff was a corporation, duly organized and existing under the laws of the state; and that the plaintiff had constructed its railroad from Easton Bay, in Talbot County, to the town of Vienna, in Dorchester County, before the first of January, 1891; and that, in the construction of its road, the plaintiff had expended large sums of money, and created a large indebtedness, still outstanding at the time of this suit brought, to wit, the 12th day of August, 1891. It was also admitted, that, before this suit was brought, the defendant received from the secretary of the plaintiff, a letter calling on him to pay the money alleged to be due on the stock, and further, that before the bringing of this suit neither the plaintiff, nor any one in its behalf, ever offered or tendered the certificates for the stock subscribed for by the defendant. The plaintiff then offered in evidence a subscription book, purporting to be a subscription book for the stock of the plaintiff, and proved by an agent of the company, to whom the book had been entrusted to procure subscriptions, that it was the subscription book of the plaintiff, and that the entry in that book, to which the name of the defendant was subscribed, was made and signed by the defendant. In that book there is this heading: "We, the undersigned, agree to subscribe to and pay for the number of shares of the capital stock of the Baltimore and Eastern Shore Railroad Company, set opposite our names, provided the said road shall be built on the Vienna route; said shares of stock to be of the par value of fifty dollars, and the same to be paid for in instalments of twenty per cent., as any ten miles of road are completed." This

delphia &c. R. Co. v. Conway (1896) 177 Pa. St. 364, 35 Atl. 716; *Blodgett v. Morrill* (1848) 20 Vt. 509.

Cf. Meyer v. Blair (1888) 109 N. Y. 600, 17 N. E. 228, 4 Am. St. 500 (distinguishing principal case); *Morgan v. Struthers* (1888) 131 U. S. 246, 33 L. ed. 132, 9 Sup. Ct. 726. See also *Winston v. Dorsett &c. Paving Co.* (1889) 129 Ill. 64, 21 N. E. 514, 4 L. R. A. 507n.

As to the admissibility of parol evidence to show that a subscription absolute on its face depended upon a condition, see *Corwith v. Culver* (1873) 69 Ill. 502, esp. p. 506; *Philadelphia &c. R. Co. v. Conway*, *supra*, at p. 368.—Eds.

heading had appended to it about sixty signatures; and then follows this entry:

"I hereby agree to take twenty shares of the Baltimore & Eastern Shore Railroad stock when completed to Vienna.

\$1,000.00.

ALBERT WEBB."

To the offer of this subscription book, with the entry therein signed by the defendant, the latter objected, and in support of his objection has assigned several grounds: First, that there was no evidence of a tender of certificates of stock to the defendant, and that this suit could not be maintained without such tender; and that the subscription was invalid because the statutory instalment was not paid. Secondly, that there was no contract of a present subscription for stock, but, at most, nothing more than a mere promise to subscribe when the road was completed to Vienna. Thirdly, that if the entry signed by the defendant be treated as a present subscription to stock, the contract is within the provisions of the Statute of Frauds, 29 Car. 11, c. 3, sec. 17, and that it is fatally defective in omitting to name the vendor of the stock, and that there is no sufficient consideration for the defendant's undertaking shown on the face of the subscription paper. There is also a general objection taken to the admissibility of the subscription book in evidence. The objection to the admissibility of the evidence was overruled.

In the opinion of this Court, none of the grounds assigned in support of the objection taken, can be sustained.¹²

* * * * *

2. The subscription in the form in which it was made was inchoate and conditional. It was such, however, as the company had a right to accept. *Taggart vs. The West. Maryland*, 24 Md. 595; *Phil. & West Chester Railroad Co. vs. Hickman*, 28 Penn. St. 318. It was simply a continual offer by the defendant to become a stockholder after the condition specified had been performed by the company. The performance of the condition precedent on the part of the company was necessary to a valid acceptance of the offer thus made by the subscriber; and before this acceptance, by the performance of the condition precedent, the defendant did not, by virtue of such subscription, become a member of the company. His subscription was a mere offer, and unless withdrawn before the condition performed by the company, it became final and absolute immediately upon the performance of the condition; or as said by this Court in *Taggart vs. West. Maryland Railroad Co.*, *supra*, such conditional subscription, upon the performance of the condition, thus became ultimately an unconditional and absolute subscription. And that being the effect and operation of the subscription made by the defendant, it is quite clear that no other or further act of subscription was necessary, or contemplated by the parties, in order

¹² Opinion given on second point only.—Eds.

to convert the original conditional subscription into an unconditional and absolute subscription. The defendant appears to have declined the conditional terms embraced in the heading of the preceding subscriptions, which required the amount of the subscriptions to be paid in instalments of 20 per cent. as any ten miles of the road should be completed; and he preferred to make his subscription separate, and to make it depend upon the completion of the road to Vienna; and when the road was so made, which is admitted to have been done before this action was brought, the subscription of the defendant for the twenty shares of stock became absolute, and the price therefor thence became payable on demand of the directors of the company. This is the clear import of the subscription of the defendant. No particular form of subscription is made essential, and the present subscription is not of a formal character; yet there is enough in the paper, when read in connection with what precedes it in the same book, to show what was really intended by the parties to the contract.

*Judgment affirmed.*¹⁸

NORWICH LOCK MFG. CO. v. HOCKADAY.

1893. 89 Va. 557, 16 S. E. 877.

ERROR to judgment of the hustings court for the city of Roanoke, rendered March 14th, 1892, on a motion for judgment for money on contract, wherein the Norwich Lock Manufacturing Company, of Roanoke, Va., was plaintiff, and J. R. Hockaday was defendant. The judgment being adverse to the plaintiff company, it obtained a writ of error to this court. Opinion states the case.

FAUNTLEROY, J., delivered the opinion of the court.

The record discloses that about February 1st, 1891, a paper headed "A New and Important Industry for Roanoke," was circulated for signatures. It proceeds: "It is proposed to organize a company for the purpose of manufacturing locks, bolts, and all house hardware, and other articles of a similar character. The capital stock of the company will be from \$350,000 to \$400,000. An existing plant can be purchased at a proper valuation, and can

¹⁸ See also *McMillan v. Maysville &c. R. Co.* (1854) 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; *Armstrong v. Karshner* (1890) 47 Ohio St. 276 ("unless restrained by statute, corporations may receive conditional subscriptions to their stock at any time after their actual incorporation").

Cf. *Taggart v. Western Maryland R. Co.* (1866) 24 Md. 563, 89 Am. Dec. 760n.

See *Red Wing Hotel Co. v. Friedrich* (1879) 26 Minn. 112, 1 N. W. 827, construing a proviso as "a condition subsequent and not a condition precedent," and therefore binding.—Eds.

be moved immediately to Roanoke. It would, at Roanoke, have a decided advantage over its present location. There can be no question that securing this manufacturing plant for Roanoke will be the greatest step," &c.

The conclusion was: "We * * * hereby subscribe the amount set opposite our names, respectively, to the capital stock of the company to be formed in accordance with the provisions of the foregoing prospectus." * * * To this prospectus, or subscription-list, is subscribed the name of "J. R. Hockaday and others," (opposite) \$1,500.

The entire amount subscribed to this paper was less than the proposed minimum of capital stock, and no company has been formed in accordance with the provisions of the aforesaid prospectus. Two months and more later, a paper, dated April 25th, 1861, was circulated for signatures, headed like the first, and proceeding: "An agreement has been made with a hardware manufactory in the North to sell its plant, &c. The stockholders of the company in the North have subscribed \$200,000 to the company that is to be located on the property of the Roanoke Development Company, and the Roanoke Development Company has subscribed \$75,000. The remaining \$75,000 must be subscribed in order to secure the industry. The R. D. Company agree to donate a suitable site for the industry, for which full paidup stock shall be issued: which stock the R. D. Co. agrees to donate to the company."

This prospectus paper concludes: "We, the undersigned, each, in consideration of the subscriptions of the others hereto, and the above agreement by the Roanoke Development Company, hereby subscribe the amount set opposite our names, respectively, to the capital stock of the company to be formed in accordance with the provisions of the foregoing prospectus," &c. The name of J. R. Hockaday, or "J. R. Hockaday and others," is not among the names of the subscribers to the capital stock under this subscription-list or prospectus; and the fact in the record is that J. R. Hockaday was approached and asked to subscribe under this second prospectus, and he positively and pointedly refused to subscribe, saying that it was a different contract and scheme from the first. Under this second prospectus the lock manufacturing plant was not to be located in or at Roanoke City (as it expressly was in the first prospectus), but to be put beyond the city limits, on the opposite side of the river, and on the lands of the Roanoke Development Company, in the county of Roanoke, where its principal office was to be located. The charter under which the plaintiff company was organized was granted by the judge of the circuit court of Roanoke county May 21st, 1891, upon the presentation and provisions of a paper dated May 11th, 1891, and signed by Arthur C. Denniston, Edw. C. Pechin, Arthington Gilpin, S. W. Jamison and P. L. Terry, purporting to be their agreement to become a corporation by the name of the "Norwich Lock Manufacturing Company, of Roanoke, Vir-

ginia," for the purpose of manufacturing, dealing in, and selling locks, &c., and other articles of house hardware, and all other articles composed of iron, wood and other substances; of erecting and conducting all buildings and structures, and the machinery and appliances and fixtures incident thereto; of acquiring, holding and selling iron and other metals, wood and other substances; of acquiring and disposing of mineral and other lands in fee, timber and timber rights, water and water-power, and privileges, &c., as may be convenient for the business of the company; of erecting houses, &c., for the purposes of its business; of making and using all roads, &c., with power to borrow money, and create, issue and sell or dispose of its bonds, and to secure the same by deed of trust, &c. The minimum capital to be \$350,000, the maximum \$500,000. The county of Roanoke to be the place where the principal office of the company is to be kept.

The Norwich Lock Manufacturing Company, the plaintiff in this suit, which was organized, under the foregoing charter, August 4th, 1891, was not formed in accordance with the provisions of the prospectus or subscription paper on which the defendant, Hockaday, subscribed, but differs therefrom, radically and materially, in essential general object and purpose, as well as in special details, powers, and provisions.

The location, which was, by the subscription paper which the defendant, Hockaday, signed, in February, 1891, to be immediately placed in the city of Roanoke, is by the charter, and terms and agreement with the Roanoke Development Company, to be on the lands of that company, lying extensively on the opposite side of the Roanoke river, outside of the limits of Roanoke City, and in the county of Roanoke. The maximum capital stock, which was to be \$400,000, is, by the prospectus which Hockaday expressly refused to sign or to recognize, and by the charter under which the plaintiff company long subsequently organized, put at \$500,000. And the purposes and powers of the company, as set forth in the prospectus and the charter under which they organized, are wholly and essentially different, embracing almost any and every industrial and speculative enterprise, whilst those specified and embraced in the prospectus or subscription signed by the defendant, Hockaday, and others, are, carefully and guardedly, expressly limited to the "purpose of manufacturing locks, bolts, and all house hardware, and other articles of a similar character."

The subscription-list which J. R. Hockaday and others signed in February, 1891, shows that the total amount of stock subscribed for, up to the day of the trial, was less, by \$20,900, than the minimum capital stated in the prospectus or subscription contract signed by "Hockaday and others." There is no evidence in the record that the defendant, Hockaday, ever signed any but the subscription paper circulated in February, 1891; that he ever attended or heard of any meeting of stockholders, or paid any part of his conditional sub-

scription, or expressly or impliedly promised to do so, or knew of or in any way acquiesced in the wide and material variances between the charter and the paper which he had signed; while it is explicitly in evidence that he refused to sign, or in any way recognize, the paper which was substituted therefor, and sued upon in this case.

After the evidence was all in, the court, on motion of the defendant, instructed the jury "that the contract of subscription signed by the defendant, and proven in this case, is conditional upon the due organization of a company under and by virtue of said contract, and in accordance with the provisions thereof; and that the Norwich Lock Manufacturing Company, of Roanoke, chartered by the Hon. Henry E. Blair, judge of the circuit court of Roanoke county, Virginia, and introduced in evidence, is not such a company as is contemplated by and provided for in said contract. That the contract of subscription by the defendant proven in this case is a conditional one—conditioned upon the organization of a company under and in accordance with the provisions of the said contract; and if they believe, from the evidence, that the plaintiff company was not organized under said contract and in accordance therewith, they must find for the defendant."

The jury did find for the defendant, and the court refused to set the verdict aside, and entered judgment accordingly.

Upon the facts in the case we can conceive of no instructions more proper, and less calculated to mislead the jury, than those given in this case. It is indisputably the province and the duty of the court to construe and instruct the jury as to the legal effect of all written instruments which are the subject of the controversy and the bases of the suit; and the court only exercised its legitimate function in comparing the subscription paper and the charter of the company under which they organized, and telling the jury that the latter was not, in legal effect, in accordance with the provisions of the former; that the plaintiff, Norwich Lock Manufacturing Company, was not such a company, nor *the* company, contemplated by and provided for in the subscription contract signed by the defendant. The charter, and the prospectus under which they organized, and to which the defendant positively refused to accede or consent, differ from the mere subscription-list signed by the defendant, as to the location, the maximum capital, and the objects and scope of the enterprise; and the company proposed to be formed, to whose capital stock he conditionally subscribed, was never formed.

There is no question in this case of amendments to the charter, whether material or immaterial. The prospectus to which the defendant subscribed his name, conditionally, was substituted by another and a radically-different prospectus (to which he refused to subscribe), and by agreement and arrangement between parties with whom he had no privity; and the substitution and changes made in the scheme and scope of the enterprise were made before

the charter was granted or applied for. If, after one has signed a contract agreeing to form a corporation for a named purpose, such contract is changed in any way, before the incorporation, without such subscriber's consent, he is not bound, because the company formed is not the company he subscribed to. 1 *Lawson R. R. & P.*, sec. 441; *Dorris v. Sweeney*, 60 N. Y. 463; *Dutchess, &c., v. Moffett*, 58 N. Y. 397; *Southern Hotel Co. v. Newman*, 30 Mo. 118; *Richmond Fac. Asso. v. Clarke*, 61 Maine 351; *Mohan v. Wood*, 44 Cal. 462.

In 1 *Lawson R. R. and P.*, section 435, p. 777, it is said: "One who signs a mere subscription paper, agreeing to take a number of shares in a corporation to be formed, is not liable therefor after the formation of the company," where the company is formed not in accordance with the provisions of the subscription paper. "One who signed, with others, a subscription paper, promising to take and pay for shares in a joint-stock association to build a hotel, most of which subscribers were afterwards incorporated, but the defendant was not one of them, is not bound, by his subscription, to pay for his shares to the corporation, there being no privity of contract." *Machias Hotel Company v. Coyle*, 58 Am. Dec. 712; *Mount Sterling Coal-Yard Company v. Little*, 16 Bush. 429.

As before said, there is no question in this case of amendments to charter; but, even after a corporation has been organized under its charter, its charter cannot be materially amended, to bind a stockholder, without his consent. To vary the route of a railroad, shortening the line, allowing business to be commenced before the full capital stock is subscribed, are instances of material changes which will release a stockholder. See note 1, sec. 500, p. 518, *Cook on Corporations*. To superadd a new and different business to the original undertaking will work a dissolution of the contract. *Clearwater v. Meredith*, 1 Wall. 40.

In *Fry's Executor v. Lexington & Co.*, 2 Metcalf (Ky.) 314, the court said: "Each stockholder has a right to insist on the prosecution of the particular objects of the charter." The stockholder may say: "I have agreed to become interested, and have contracted, in view of the profits expected, and the perils and losses incident to that description of business; but I have not agreed that those to be intrusted with the capital I contributed shall have power to use it in a business of a different character, and attended with hazards of a different description." *Marietta, &c., R. R. Co. v. Elliott*, 10 Ohio St. Rep. 57 (1859); *Ashton v. Burbank*, 2 Dill. 435 (1873).

There is no evidence, or even a contention, that the defendant ever signed any subscription paper but the prospectus or subscription-list No. 1, in February, 1891, which was abandoned and substituted by the prospectus and agreement dated May 11th, 1891; that he ever attended or heard of any meeting of stockholders, or paid any part of his alleged subscription, or expressly or impliedly promised to do so, or in any way acquiesced

in the variances between the charter and the paper he had signed; but there is undenied evidence that he positively refused to sign the paper which was substituted therefor. And the record plainly shows that there was in evidence before the jury the all-sufficient defense against the plaintiff's claim—viz., that, up to the trial, the plaintiff company had failed to obtain subscriptions to the extent of even its minimum of capital stock; and, therefore, it could not lawfully hold the defendant liable for his mere conditional subscription, even though the scheme and scope of the business proposed in the first prospectus had not been radically and essentially changed and enlarged by the second and substituted prospectus, to which defendant was not a party or privy. Cook on Corp., sec. 176, says: "It is an implied part of a contract of subscription that the contract is to be binding and enforceable against the subscriber only after the full capital stock of the corporation has been subscribed." He cannot be even liable to assessment unless and until the proposed capital stock of the company has been fully subscribed, unless there is a contrary provision in the article, or in the general law under which the corporation is formed. 1 Lawson R. R. and P., sec. 439, p. 733; Morawetz on Corp., sec. 259.

The rule of the Code of 1887, sec. 3484, applied to the evidence certified in this record, requires that the verdict of the jury, which is fully warranted by the facts and the law, and the judgment of the court thereon, should be affirmed.

*Judgment affirmed.*¹⁴

¹⁴ In the following cases material departures from the original purpose or scheme were held to release the subscribers. *Knox v. Childersburg Land Co.* (1888) 86 Ala. 180, 5 So. 578 (statutory modification pending organization of the system of payment for shares); *Board v. Mississippi &c. R. Co.* (1859) 21 Ill. 337 (project to construct one continuous railroad across the state changed so as to divide same into three distinct parts); *Middlecote Hotel Co. v. Yeomans* (1899) 89 Ill. App. 170 (capital fixed at \$30,000 instead of \$25,000); *Champion v. Memphis &c. R. Co.* (1858) 35 Miss. 692 (substantial deviation from proposed route of railroad); *Dorris v. Sweeney* (1875) 60 N. Y. 463 (agreement to take stock in corporation to preserve fruit by a patented process, corporation actually formed to manufacture all preserved fruits and to can fruits and other products); *Woods Motor Vehicle Co. v. Brady* (1905) 181 N. Y. 145, 73 N. E. 674 (object of proposed company was "dealing in automobiles and motor vehicles," corporation as organized was to engage in "The manufacturing, leasing, purchasing and selling of all kinds of automobiles, motor vehicles and other vehicles"); *Comanche Cotton Oil Co. v. Browne* (1905) (Tex. Civ. App.) 90 S. W. 528, reversed (1906) 99 Tex. 660, 92 S. W. 450; *Greenbrier Industrial Exposition v. Rodes* (1893) 37 W. Va. 738, 17 S. E. 305 (change in corporate duration); *West End Real Estate Co. v. Nash* (1902) 51 W. Va. 341, 41 S. E. 182; *Smith v. Burns &c. Mfg. Co.* (1907) 132 Wis. 177, 111 N. W. 1123 (conditions of repudiation considered); *Ashton v. Burbank* (1873) 2 Dill. C. C. (U. S.) 435 (fire, marine and inland insurance added to life and accident insurance); *Stewart's Case* (1866) L. R. 1 Ch. App. 574.

Cf. Olympia Mining Co. v. Kerns (1907) 13 Idaho 514, 91 Pac. 92; *Haskell v. Worthington* (1887) 94 Mo. 560, 7 S. W. 481; *Auburn Bolt &c. Works v. Shultz* (1891) 143 Pa. St. 256, 22 Atl. 904.

For examples of changes held not to release a subscriber, see *Banet v. Alton*

CHETLAIN v. REPUBLIC LIFE INS. CO.

1877. 86 Ill. 220.

APPEAL from the Circuit Court of Cook County; the Hon. E. S. Williams, Judge, presiding.

MR. JUSTICE WALKER delivered the opinion of the Court:

The Republic Life Insurance Company was incorporated by an act of the General Assembly of this State, and became organized, and entered upon the business for which it was created. Appellant's intestate became a subscriber for 500 shares of \$100 each of its capital stock; and as a payment of twenty per cent thereon the company permitted him to execute his notes therefor, drawing interest, payable five years after date, and he executed a deed of trust on property in the city to secure the payment of principal and interest. Walker, in his life-time, paid \$400 of interest on this indebtedness. Having died intestate, appellant was duly appointed the administrator of his estate, and, the money not having been paid, appellee filed a bill against the administrator, widow, and heirs of Walker, to foreclose the deed of trust, and subject the trust property to sale for the payment of this indebtedness.

Answers and a cross-bill were filed, and a trial was had on the original bill, answers, replications, exhibits, and proofs. The court found that there was due on the notes, for principal and interest, the sum of \$14,357.30, and ordered its payment in ten days, and, in default thereof, that the premises be sold, subject to redemption, and the proceeds of the sale be applied to discharge the decree, and, if not sufficient, that the unpaid balance be paid in due course of administration. From that decree the administrator appeals.

In defense it is urged that the company misappropriated their funds by purchasing the stock, etc., of the National Life Insurance Company; in purchasing a building at a price beyond the wants and means of the company, which impaired the value of Walker's stock; and because the company reduced the amount of its capital stock. This is a statement of the grounds relied on as a defense.

That there was a sufficient consideration to support these notes at law there would not seem to be the slightest doubt. And the question is presented whether the consideration has failed, or whether for any reason it has become inequitable to enforce the payment of this money.

The mere mismanagement of the affairs of a corporation has never been held to release stockholders or others from their obligations to the company. When Walker purchased and became the owner of this stock—whether paid for in money, notes, or otherwise—he became entitled to all the privileges and benefits of a stockholder, and liable to all the burdens the relation imposes. Had there

been dividends, he would have been entitled to share in them. Had there been losses imposing liabilities on stockholders, he would have been required to respond to them.

The stockholders are the owners of the franchise, property, and assets of the company which remain after its debts and liabilities are discharged. For convenience in the transaction of business, and to carry out the purposes of the organization, the charters of such bodies usually authorize the stockholders to choose a certain number from among themselves, as directors, who are empowered to transact its business and exercise its franchises. And in doing so they are agents or trustees for the stockholders, and the latter are bound by their acts within the scope of their authority. When their acts are outside of, and beyond, the scope of their authority, the stockholders are not bound by such acts, and may, no doubt, in a reasonable time, proceed in equity to have the act canceled, and their rights protected from injury and loss growing out of the unauthorized act. If, in this case, the purchase of the house from Farwell was *ultra vires*, or even an abuse of power, any stockholder might have filed his bill to enjoin its purchase, or, if having been purchased without authority, in a reasonable time afterwards, to cancel the purchase and have the consideration which had been paid restored to the company.

Directors, like any other trustees, may be restrained from the performance of unauthorized acts, or to rescind and cancel them when performed. And the stockholders, occupying the relation of cestuis que trust, may invoke the aid of equity to thus protect their interests. In this case the house was purchased in Walker's life-time, and more than two and a half years before his death, and some five months after he became a stockholder. Yet he took no steps to avoid the purchase, and have the money and stock paid for it restored to the company. Nor do we see that he ever even objected to this purchase; and we presume he did not, if for no other reason, because it seems to have been a profitable investment, as it was afterward sold to the National Life Insurance Company for half a million dollars. It is therefore, contrary to these rules to hold that whilst Walker, as a stockholder, acquiesced in, if he did not approve of, this purchase, and seems, from his non-action, to have been willing to take the chances of securing profits thereby, he is to be heard now, or his administrator for his estate, to set this up as a defense to the collection of the purchase money for his stock. This is the scope of what was said in regard to equitable relief in the cases of *Hays v. Ottawa, Oswego and Fox River Valley Railroad Company*, 1 Ill. 424, and *Ottawa, Oswego and Fox River Valley Railroad Company v. Black*, 79 id. 262. These cases do not, nor were they intended to, hold that a debtor to the company, whether a stockholder or other person, could resort to equity and be discharged from his obligation, because the directors have acted beyond their power or in its abuse.

What has been said in reference to the purchase of the house, and the rules announced in the cases above referred to, fully govern and dispose of the question in reference to the purchase of the stock of the National Life Insurance Company. If it was ultra vires, then the act was simply void, and Walker in his life-time, or his administrator after his death, in a reasonable time, if they believed the purchase unauthorized, might have filed a bill to set the whole transaction aside, and restore appellee to its previous condition. This transaction seems to have occurred two months or more before Walker's death, yet he took no such steps, nor has appellant since that time. This, then, forms no defense to the collection of these notes. * * *

Perceiving no error in the record, the decree of the court below is affirmed.

*Decree affirmed.*¹⁵

KENOSHA ETC. R. CO. v. MARSH.

1863. 17 Wis. 13.

APPEAL from the Circuit Court for Kenosha County.

The case is stated in the opinion of the court so far as is necessary for an understanding of the only point decided. The circuit court, on motion of the defendant, nonsuited the plaintiff.

PAINE, J.—This action was brought upon a subscription to the capital stock of a railroad company chartered to build a road from the city of Kenosha to Beloit. Ch. 60, Pr. Laws of 1853. Afterwards, by Ch. 22, Pr. Laws of 1857, the legislature changed the enterprise from that of building a road to Beloit, to one of building a road to the state line between this state and Illinois, at or near Genoa, in Walworth county. This change was obtained by the company, which acted under it, and, under still another law, consolidated with an Illinois company, which was authorized to build a road from

¹⁵ *Accord*, Ottawa &c. R. Co. v. Black (1875) 79 Ill. 262; Proprietors v. Dickinson (1856) 6 Gray (72 Mass.) 586; United States Vinegar Co. v. Foehrenbach (1895) 148 N. Y. 58, 42 N. E. 403; Caley v. Philadelphia &c. R. Co. (1876) 80 Pa. St. 363; Cartwright v. Dickinson (1889) 88 Tenn. 476, 12 S. W. 1030, 7 L. R. A. 706, 17 Am. St. 910. In the case last cited, Lurton, J., said: "That the corporation has been guilty of a violation of its charter, in this or any other matter, is no defense to an action for calls due from a shareholder upon his shares. His remedy was against the corporation to restrain such alleged illegal action, or is against the agents personally, for any wrong and injury done him. It furnishes no reason why he shall not carry out his own contract" (p. 488).

That abandonment or sale of part of enterprise, e. g. railroad, constitutes no defense, see Phoenix Warehousing Co. v. Badger (1876) 67 N. Y. 294; Armstrong v. Karshner (1890) 47 Ohio St. 276, esp. 300, 24 N. E. 897. Cf. South Georgia &c. R. Co. v. Ayres (1876) 56 Ga. 230 (sale of railroad).—Eds.

Rockford in that state to the same point on the state line. This action was brought by the consolidated company.

After the evidence of both parties had been introduced, the defendant moved for a nonsuit, for the reason, among others, that this was such a radical change in the enterprise as released him from his subscription. The motion was granted upon another ground, but we think it was properly granted upon this.

Considered independently of the effect of the power reserved in our constitution to the legislature, to amend or repeal the charters of all incorporations, all authorities concur in stating the general rule to be, that a radical, fundamental change in the character of the enterprise releases the stock subscriber who does not assent. In applying this rule many cases are found where the particular change made was held not to be of this character. But we think the plain implication from the reasoning in all of them is, that a change like the one here in question would be so held. Thus in *Banet v. R. R. Co.*, 13 Ill. 504, the change made only straightened the original route, leaving it between the same termini. The court held that this was not a radical change, but that it left the enterprise substantially unchanged. But they say expressly that if the change had been to authorize a road from Alton to Vandalia, or Shelbyville, it would have been a different enterprise. But it will be seen by a reference to the map that a change to a road from Alton to Shelbyville would have been very similar to the one made here. The road as changed here runs in a line entirely southwest of the original route, and to a point only about half as far as Beloit. Within the reasoning of all the cases, we think this is a change from one enterprise to another, and not one which leaves the original enterprise substantially remaining.

The supreme court of Indiana has recently held that the mere consolidation with another company under an act of the legislature releases nonassenting subscribers. *McGray v. R. R. Co.*, 9 Ind. 358; *Booe v. R. R. Co.*, id., 93. I should not wish to adopt that conclusion without further examination, for although it may be within the principle of *R. R. Co. v. Croswell*, 5 Hill 383, and other cases of a similar character, still there seems to me to be a fair distinction between such changes as only add something to the original enterprise, which becomes tributary to it, and makes its operation more perfect and successful, and changes which abandon the original undertaking for a new one. There is certainly some ground for saying that changes of the former character may be deemed to be fairly within the scope of the original object, as it may reasonably be assumed that every association which undertakes the accomplishment of a particular enterprise, intends to make such changes as experience may show to be necessary for its most successful prosecution. And if this may be assumed, then, although such changes were of course not originally provided for, yet they may fairly be regarded as so far incidental to the original purpose as to be within the scope of the authority which each member has con-

ferred upon the corporation, to bind him by its action whenever the necessary legislative assent is obtained. And if this can be regarded as a correct rule, I should not be prepared to say that a consolidation with another company whose road ran from either terminus in the same general direction, or the connection of a line of steamboats with the road, when one of the termini was on navigable waters, if authorized by the legislature and assented to by the corporation as a body, ought to release a stockholder who did not assent. These things are totally different in their nature from a change which abandons the original enterprise entirely. These cases go, therefore, much further than it is necessary to go here. The following cases also sustain the conclusion that such a change as was made here releases subscribers not assenting: *Plank Road Company v. Arndt*, 31 Penn. St. 317; *Hester v. Memphis and Charleston R. R. Co.*, 32 Miss. 378. The following cases, as stated in the digest, sustain the same rule, though the volumes have not yet arrived in our library: *Champion v. Memphis R. R. Co.*, 35 Miss. 692; Vol. 20 U. S. An. Dig., p. 219, sec. 222; *Witter v. Miss., etc., R. R. Co.*, 20 Ark. 463; Vol. 20 U. S. An. Dig., p. 219, sec. 235. See, also, *Fry's Ex'rs v. R. R. Co.*, 2 Met. (Ky.) 314.

The question then remains, whether the powers reserved in the constitution to amend, alter or repeal charters should prevent that effect. Some of the cases seem to place great stress upon the existence of this power, and to intimate that under it the nonassenting stock subscriber may be bound by a change, the effect of which would otherwise be to release him. I am wholly unable to see that it should have any such effect. The occasion of reserving such a power either in the constitution or in charters themselves is well understood. It grew out of the decisions of the supreme court of the United States, that charters were contracts within the meaning of the constitutional provision that the state should pass no laws impairing the obligation of contracts. This was supposed to deprive the states of that power of control over corporations which was deemed essential to the safety and protection of the public. Hence the practice, which has extensively prevailed since those decisions, of reserving the power of amending or repealing charters. But this power was never reserved upon any idea that the legislature could alter a contract between a corporation and its stock subscribers, nor for the purpose of enabling it to make such alteration. It was solely to avoid the effect of the decision that the charter itself was a contract between the state and the corporation, so as to enable the state to impose such salutary restraint upon these bodies as experience might prove to be necessary. But I suppose it would hardly be claimed that the state, even where this power of amendment is reserved, could, by amending the charter of a railroad company so as to provide for a new and entirely different road, impose any obligation on the corporation to build it. It might possibly repeal the old charter, but whether the company would undertake the enterprise provided for in the amendment, would still depend en-

tirely upon its own consent, as it is well settled that a grant of corporate franchises cannot be imposed upon any persons against their consent any more than any other grant. Undoubtedly the legislature might, under the power, impose new duties and new restraints upon corporations in the prosecution of the enterprises already undertaken. And provisions of this nature would be binding whether assented to or not. But when it comes to a question of embarking in a new enterprise, the legislature cannot impose this as a duty upon any corporation. All it can do is to grant it the power, and then it is for the corporation to accept it or not, as it pleases. So that, in all cases where charters are changed, the right to bind stock subscribers who do not assent, seems to me to derive no additional support from the fact that the power of amending the charter has been reserved, but to depend essentially upon the question whether the change is of such a character that it may be deemed so far in furtherance of the original undertaking, and incidental to it, as to be fairly within the power of the corporation to bind its individual members by its corporate assent, or whether it is such a departure from the original purpose that no member should be deemed to have authorized the corporation to assent to it for him. If I am correct in supposing that an amendment authorizing an entirely different road would not be binding on a corporation without its own assent, it must follow that the question whether any particular subscriber is bound must depend upon the question whether he has himself assented, or whether the rest could bind him by their assent, and not on the question whether the legislature had power to pass the amendment.

The result of my views upon this point is, that an amendment of this kind, merely authorizing the substitution of a new enterprise for the old, has precisely the same effect that it would have had if there had been no power reserved to amend the charter. The legislature does not profess to make it obligatory. They grant it as a power to be accepted if the company chooses to accept it; otherwise not. This is just what they might have done if the power of amendment had not been reserved. And it seems to me that the question whether an individual subscriber was bound or not by the corporate assent, should be determined by the same principles in either case. The power of amendment was never reserved with reference to any question between the corporation and its stock subscribers, but solely with reference to questions between the corporation and the state, when the latter desired to make compulsory amendments against the wish of the former.

The effect of this reserved power is discussed in the matter of *Oliver Lee & Co.'s Bank*, 21 N. Y. 20, 21, by Judge Denio. The amendment there made did not attempt to change the corporate enterprise, but belonged to the class I have referred to, of amendments designed for the better protection of the public. It was a case where new liabilities were imposed on the stockholders, arising from the continued exercise of the corporate powers originally conferred.

There being, therefore, no question in the case of a radical change of the original enterprise, I cannot think the judge intended that his remarks should be applicable to such a case. I cannot think that he intended to say that any person who subscribes for the stock of a corporation chartered for a special enterprise, where the power to alter or amend the charter is reserved by the legislature, has thereby agreed that the legislature and the majority of his associates may, without his consent, transfer his investment to a totally different project. Indeed that this could not be done is fairly implied from a subsequent opinion of Judge Denio, in *The Plank Road Company v. Griffin*, 24 N. Y. 156. There the company was originally chartered to build a plank road. Afterwards a law was passed extending the time in which they were allowed to finish it by laying down plank, and allowing them, in the meantime, to erect toll gates and exercise the rights of turnpike companies. The judge says: "It is certainly possible that this act was obtained simply as a cover for abandoning the plan of a plank road, and to enable the directors to establish a turnpike. This, however, is not the presumption of the law. On the face of the enactment it simply conferred on the corporation an indulgence which it would not otherwise possess, of postponing the completion of the road for a considerable time, and of so managing it that it should be a source of profit in the meantime. I think that this was within the scope of the reservation contained in the general act which declares that the legislature may at any time alter, amend or repeal it, and may amend and repeal any corporation which may be formed under it."

This plainly implies that if the act had abandoned the original project, the subscriber would not have been bound. For the judge had no occasion to make the argument he did to show that the change was within the scope of the power of amendment, if the power was unlimited.

Pierce, in his work on railroads, p. 98, gives it as the result of the authorities, that even when the power of amending is reserved, it is not unlimited, but "that such a radical change in the company as diverts it from its original purpose" is not binding on a dissenting shareholder. But if the power is not unlimited, where is the limit? By what principles is it to be established? I know of none except those I have already contended for, which base the right upon the implied authority conferred by each one who becomes a member of the corporation, on the majority, to bind him by such changes as may fairly be regarded as incidental to the original project.

*The judgment must be affirmed.*¹⁰

¹⁰ *Memphis &c. R. Co. v. Sullivan* (1876) 57 Ga. 240; *Snook v. Georgia Improvement Co.* (1889) 83 Ga. 61, 9 S. E. 1104; *Oldtown &c. R. Co. v. Veazie* (1855) 39 Maine 571 (*semble*); *Rutland &c. R. Co. v. Thrall* (1863) 35 Vt. 536 (*semble*). *Accord.* But see *Sprague v. Illinois &c. R. Co.* (1857) 19 Ill. 174; *Terre Haute &c. R. Co. v. Earp* (1859) 21 Ill. 291.

In *SCHENECTADY &c. PLANK ROAD CO. v. THATCHER* (1854) 11 N. Y. 102,

held that a stockholder was not released from his subscription by the corporate acceptance of a subsequent legislative act, enacted under the reserved power to amend, increasing the corporate capital and authorizing the construction of a branch-road, though without his consent express or implied. Johnson, J., said: "The first section of the act of 1847 subjects the corporation founded under its provisions to the 3d and 4th titles of chapter 18 of the first part of the revised statutes. One of these is that the charter of every corporation that shall hereafter be granted by the legislature shall be subject to alteration, suspension and repeal, in the discretion of the legislature. This condition is thereby engrafted upon the original constitution of companies formed under the act. The subsequent act was passed and operates under that reservation of power to the legislature. The corporate property is subject to that power, by reason of the assent to its exercise, implied from and by an organization under the act which reserves it. Every one who enters into such a company is aware of the reservation of the power and of the possibility of its exercise and trusts, as in many other matters he must trust, to the wisdom and justice of the legislature that this power will not be abused" (p. 114).

In *BUFFALO & C. R. Co. v. DUDLEY* (1856) 14 N. Y. 336, at 354-5, Selden, J., said: "The point made by the defendant upon the alteration of the plaintiff's charter, changing the name of the corporation and authorizing the extension of its road from Attica to Buffalo, must, I think, be considered as sufficiently answered by the decision of this court in the case of *The Schenectady and Saratoga Plank Road Company v. Thatcher* (1 Kern., 102). The power reserved to the legislature in the original act of incorporation, to alter or repeal the act, is as broad in this case as in that. It is, indeed, entirely unlimited. Under the rule established in that case, no mere addition to or alteration of the charter, however great, would operate to discharge a stockholder from his obligation to the corporation. To work such a discharge the charter must be repealed, or the legislation must be such as virtually to subvert the corporation itself; or, at least, to destroy its identity."

See note, 7 Columbia Law Rev. 598-601.

That an amendment extending time for construction is not fundamental, see *Taggart v. Western Maryland R. Co.* (1866) 24 Md. 563, 89 Am. Dec. 760n; *Union Hotel Co. v. Hersee* (1880) 79 N. Y. 454, 35 Am. Rep. 536. See also *Mercantile Statement Co. v. Kneal* (1892) 51 Minn. 263, 53 N. W. 632.

[SUBSCRIPTIONS INDUCED BY FRAUD OR MISREPRESENTATION.—There is no question but that a subscriber may defend as against the corporation on these grounds. The only, and the important, question is whether he can so defend as to impair the rights of creditors; see subject of "Creditors", *infra*. On this general topic, particularly the right of rescission, the degree of diligence required, and the effect of insolvency, see *Ashley's Case* (1870) L. R. 9 Eq. 263; *Newton Nat. Bk. v. Newbegin* (1896) 74 Fed. 135, esp. 139-142, 20 C. C. A. 339, 33 L. R. A. 727; *Gress v. Knight* (1910) 135 Ga. 60, 68 S. E. 834, 31 L. R. A. (N. S.) 900n, and comment, 10 Columbia Law Rev. 771, 24 Harvard Law Rev. 147. See also Machen's *Modern Law of Corporations*, §§ 204-219.—Eds.]

CHAPTER VII.

DIRECTORS.

Section 1.—Powers—Stockholders' Control.

COMMERCIAL NATIONAL BANK v. WEINHARD.

1903. 192 U. S. 243, 48 L. ed. 425, 24 Sup. Ct. 253.

THESE actions were brought in the Circuit Court of the State of Oregon for Multnomah County upon separate demands to recover the value of stock severally held by Weinhard and Williams in the Commercial National Bank of Portland, Oregon; Williams owning sixty shares of the par value of \$6,000, and Weinhard one hundred shares of the par value of \$10,000. By stipulation the cases were heard together in the circuit court; a jury being waived and a trial had to the court. The cases were considered together as one appeal in the Supreme Court of Oregon, which affirmed the judgment of the lower court, 41 Oregon 359, assessing the value of the stock and giving judgment in favor of the plaintiffs, now defendants in error.

The Commercial National Bank of Portland was duly organized under the National Banking Act, and carried on business in the city of Portland, Ore. It appeared that the capital of the bank had become impaired, and thereupon such proceedings were had that on December 5, 1896, the Comptroller issued the following notice to the bank:

"Treasury Department,
"Office of Comptroller of the Currency,
"Washington, D. C., December 5, 1896.

"Whereas, It appears to the satisfaction of the Comptroller of the Currency that the capital stock of the Commercial National Bank, Portland, Oregon, had become impaired to an extent which makes necessary an assessment of two hundred and fifty thousand dollars (\$250,000) upon the shareholders of said association to make good such deficiency:

"Now, therefore, notice is hereby given to said association, under the provisions of section 5205 of the Revised Statutes of the United States, to pay the said deficiency in its capital stock by assessment upon its shareholders, pro rata, for the amount of the capital stock held by each, and if such deficiency shall not be paid, and said bank shall refuse to go into liquidation, as provided by law, for three

months after this notice shall have been received by it, a receiver will be appointed to close up the business of the association, according to the provisions of section 5234 of the Revised Statutes of the United States.

"In testimony whereof, I have hereunto subscribed my name and caused my seal of office to be affixed to these presents, at the Treasury Department, in the city of Washington, and District of Columbia, this 5th day of December, A. D. 1896.

"JAMES H. ECKLES,
"Comptroller of the Currency.

"To the Commercial National Bank, Portland, Oregon."

After receipt of this notice, upon December 12, 1896, the board of directors passed this resolution:

"Resolved, That in accordance with the notice served upon this association by the Comptroller of the Currency, under date of December 5, 1896, and received by this bank on the 11th day of December, 1896, an assessment is hereby levied upon the shareholders of this bank of fifty per cent, or \$50 per share, payable at this bank on or before March 11, 1897.

"And, Resolved, That the cashier of this bank be, and he hereby is, authorized and instructed to serve upon each shareholder of the bank a legal notice of the above assessment by sending such notice to each shareholder's address by registered mail."

Upon December 17, 1896, notice of this assessment was served upon each of the stockholders of the bank. The defendants in error having failed to pay this assessment, on March 18, 1897, the board of directors passed a resolution directing the sale of the delinquents' stock to be made at public auction on May 5, 1897. In pursuance of this order, and on the day named, the stock was sold for the amount of the assessment. The Federal question is whether the board of directors in thus assessing and selling the stock of the defendants in error exceeded their powers under the National Banking Act; it being claimed that a valid assessment could only be made by the action of the stockholders, and that the sale by the directors upon this assessment was unlawful and amounted to a conversion of the stock.

MR. JUSTICE DAY, after making the foregoing statement, delivered the opinion of the court.

This case requires the construction of section 5205 of the Revised Statutes of the United States as amended. 3 Comp. Stat. 3495. The section is as follows:

"Every association which shall have failed to pay up its capital stock, as required by law, and every association whose capital stock shall have become impaired by losses or otherwise, shall, within three months after receiving notice thereof from the Comptroller of the Currency, pay the deficiency in the capital stock, by assessment upon the shareholders pro rata for the amount of capital stock held by each; and the Treasurer of the United States shall withhold the interest upon all bonds held by him in trust for any such association,

upon notification from the Comptroller of the Currency, until otherwise notified by him. If any such association shall fail to pay up its capital stock, and shall refuse to go into liquidation, as provided by law, for three months after receiving notice from the Comptroller, a receiver may be appointed to close up the business of the association, according to the provisions of section fifty-two hundred and thirty-four. And provided, That if any shareholder or shareholders of such bank shall neglect or refuse, after three months' notice, to pay the assessment, as provided in this section, it shall be the duty of the board of directors to cause a sufficient amount of the capital stock of such shareholder or shareholders to be sold at public auction (after thirty days' notice shall be given by posting such notice of sale in the office of the bank, and by publishing such notice in a newspaper of the city or town in which the bank is located, or in a newspaper published nearest thereto,) to make good the deficiency, and the balance, if any, shall be returned to such delinquent shareholder or shareholders."

The assessment in this case was made by the board of directors without any action of the stockholders of the association, and the defendants in error having failed to pay the same upon notice, their stock was sold as directed in the statute. It is claimed that an assessment by the directors without action of the stockholders was without authority of law and amounted to a conversion of the stock. This view was sustained in the Supreme Court of Oregon. The assessment ordered by the Comptroller was for the purpose of restoring the capital of the bank, and thus enabling it to continue its business. Ample power is conferred upon the Comptroller for this purpose. His action is in aid of other sections of the law preventing a withdrawal of the capital, or the making of dividends when losses have been sustained equal to the undivided profits. Sections 5202-5204, Rev. Stat. When the notice is received from the Comptroller by the bank under section 5205, the association has no authority to review or gainsay the necessity thereof. That question is concluded by the action of the Comptroller. The money to be raised for the continuance of the business may or may not be used in the liquidation of debts. The assessment is entirely different from that provided for in section 5151, calling upon the individual responsibility of shareholders for the payment of debts. Under the last named section the stockholder is required to pay such assessments as may be made, to meet the outstanding obligations of the bank, within the limit of an amount equal to the par value of the stock in addition to the amount invested therein. He has no election of payment, but is required to meet this liability, created by law for the benefit of creditors. Under section 5205 the amount paid is subject to the control of the board of directors in the continued operations of the bank. If the stockholders are to have a voice in making or declining to make the assessment, they may well hesitate to entrust more capital to the control of a board under whose management it has already been impaired. Certain powers are conferred by law upon the directors.

Section 5136 provides that the association shall have power—

"Sixth. To prescribe, by its board of directors, by-laws not inconsistent with law, regulating the manner in which its stock shall be transferred, its directors elected or appointed, its officers appointed, its property transferred, its general business conducted, and the privileges granted to it by law exercised and enjoyed."

"Seventh. To exercise by its board of directors, or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin and bullion; by loaning money on personal security; and by obtaining, issuing and circulating notes according to the provisions of this Title."

And, again, by section 5145, it is declared that the "affairs" of the corporation "shall be managed by not less than five directors."

Thus the directors are given authority to transact the usual and ordinary business of national banks. Obviously, the power conferred may be exercised in all usual transactions through the executive officers of the bank without consultation with the stockholders. In the present case the question to be dealt with is vital to the continuance of the life of the association, as only by complying with the requirement of the Comptroller in assessing a sum sufficient to make up the impaired capital of the bank can its business be continued. The shareholders by their contracts of subscription have agreed to pay in the amount of capital stock subscribed and to discharge the additional liability imposed by the statute. They have not contracted to meet assessments at the will of the directors to perpetuate the business of a possibly losing concern. It would be going far beyond the usual powers conferred upon directors to permit them to thus control the corporation. Corporate powers conferred upon a board of directors usually refer to the ordinary business transactions of the corporation. *Railway Company v. Allerton*, 18 Wall. 233. The assessment is required by the Comptroller, not by the directors. The association is to receive notice thereof, and action must be taken by the association to meet the requirements of the Comptroller under the statute. It is provided that if the association fail to pay up its capital stock, and refuse to go into liquidation, as provided by law, for three months after receiving notice from the Comptroller, a receiver may be appointed to close up the business of the association according to the provisions of section 5234. This important provision is entitled to much weight in determining the proper construction of the statute. The assessment may be avoided, and the amount required is not payable if the association decides to go into liquidation. Provision for voluntary liquidation is made in section 5220 wherein authority is given to liquidate upon a vote of shareholders owning two-thirds of the stock. Such liquidation does not prevent the assessment of stockholders under section 5151 for the benefit of creditors and the enforcement of the liability of the shareholders in

an action by a receiver or directly by the creditors. Comp. Stat. sec. 5234; sec. 2, Act of June 30, 1876, as amended, 3 Comp. Stat. 3509. The section referred to, 5234, directs the appointment of a receiver to take possession of the books, records and assets of the association, to collect the debts and claims belonging to it, and, among other things, if necessary to pay the debts of the association, to enforce the individual liability of the shareholders.

7 We are of opinion that section 5205 is intended to and does confer upon the association the privilege of declining to make the assessment to make good the deficiency to the capital, and to elect instead to wind up the business of the bank under section 5220, which provides for voluntary liquidation by a vote of two-thirds of the shareholders. The question is, who shall exercise this privilege and determine the future of the association—is it the directors or the shareholders who have this right of decision? The origin and continuation of the association would seem to be matters in which the owners and not the managers of the bank are primarily interested. If these are privileges of the shareholders and only exercisable by them, this case presents a total lack of the exertion of the power by those upon whom it is legally conferred, as no action of the shareholders was had in the present case in making the assessment. Action upon the Comptroller's order involves extraordinary action of the association, and determines its future operations or liquidation, and is not found within the powers conferred upon the directors for the management of the business of the bank. If this were not so, then the decision of a question of such vital importance is left to the directors, who may or may not be large holders of stock. As it is a matter foreign to the powers of such boards and not conferred by statute or required for the transaction of the business of the bank, we think it was intended to be vested in the shareholders. Whether a given power is to be exercised by the directors or the shareholders depends upon its nature and the terms of the enabling act. In certain instances the law specifically requires the action of the association to be taken by its incorporators or shareholders. Sections 5133, 5134, 5136, 5143, Rev. Stat. These sections regulate matters not pertaining to the ordinary business of the bank entrusted to the directors. They deal with the exercise of those powers which concern the organization of the corporation, the amount of its capital stock and kindred matters.

In section 5205 the requirement of the Comptroller is that the association make the assessment. It is the "association" which is required to pay up the stock or go into liquidation. The payment of the assessments must come from the shareholders, and we are of the opinion that the statute contemplates action upon the alternatives presented in the statute by the association composed of its shareholders. It is true, as suggested by the learned counsel for the plaintiff in error, that it requires a two-thirds vote of the stockholders to put the bank into liquidation under section 5220; but if the assessment is not carried, and the shareholders have not a two-thirds vote favoring liquidation, the bank is put in liquidation, and the shareholders' lia-

bility is the statutory one for the benefit of creditors, and not a venture of more capital in the enterprise with a possible stockholders' liability upon the liquidation of the bank, although the shareholders—the real owners of the property—be willing to make good the impaired capital and continue the business. On the other hand, if the directors may assess to make good impaired capital, the shareholder must pay the assessment or submit to the sale of his stock. Such extraordinary powers are far beyond those required in the management of the bank's affairs or conferred in the sections of the law defining those conferred upon the directors. In *Delano v. Butler*, 118 U. S. 634, 653, while the question was not directly involved, in speaking of assessments under the act, Mr. Justice Matthews, delivering the opinion of the court, said:

"The assessment imposed upon the stockholders by their own vote, for the purpose of restoring their lost capital, as a consideration for the privilege of continuing business, and to avoid liquidation under § 5205 of the Revised Statutes, is not the assessment contemplated by § 5151, by which the shareholders of every national banking association may be compelled to discharge their individual responsibility for the contracts, debts and engagements of the association. The assessment as made under § 5205 is voluntary, made by the stockholders themselves, paid into the general funds of the bank as a further investment in the capital stock, and disposed of by its officers in the ordinary course of its business. It may or may not be applied by them to the payment of creditors, and in the ordinary course of business, certainly would not be applied, as in cases of liquidation, to the payment of creditors ratably; whereas, under § 5151, the individual liability does not arise, except in case of liquidation and for the purpose of winding up the affairs of the bank. The assessment under that section is made by authority of the Comptroller of the Currency, is not voluntary, and can be applied only to the satisfaction of the creditors equally and ratably."

We concur in this reasoning. The assessment under section 5202 provides for a sum to continue the operations of the bank and if unpaid subjects the stock of the shareholders to sale to make good the deficiency in its collection. Shareholders are given the right to go into liquidation, subjecting themselves, it is true, to the liability of the assessment for the benefit of creditors under section 5151 to an amount equal to the par value of their stock, if needed to make good the indebtedness of the bank, but risking no further investment of new capital in the continued business of the bank. The choice of methods is with the shareholders, and to them is addressed the decision of the question and making of the assessment if that course is determined upon. *Hulitt v. Bell*, 85 Fed. Rep. 98. In the present case the assessment was made by the directors without action by the shareholders, and, not being within the statute, was void. It follows

that the Supreme Court of Oregon properly affirmed the judgment of the lower court in which the value of the stock sold was recovered.
*Judgment affirmed.*¹

AUTOMATIC, ETC., SYNDICATE CO., LIMITED, v.
CUNNINGHAME.

1906. L. R. (1906) 2 Ch. Div. 34.²

MOTION.

The Automatic Self-Cleansing Filter Syndicate Company, Limited, was incorporated on June 10, 1896. The original capital of the company was 700l., divided into 700 shares of 1l. each; but the capital had since been increased, and there had now been issued 2,700 shares of 1l. each.

The objects of the company, as stated in clause 3 of its memorandum of association, were (inter alia): (a) To acquire from James

¹ Mr. Justice Bradley in *Chicago City R. Co. v. Allerton* (1873) 18 Wall. (U. S.) 233, 21 L. ed. 902: "The general power to perform all corporate acts * * * does not extend to a reconstruction of the body itself, or to an enlargement of its capital stock. * * * Changes in the purpose and object of an association, or in the extent of its constituency or membership, involving the amount of its capital stock, are necessarily fundamental in their character, and cannot, on general principles, be made without the express or implied consent of the members." See also, *Clark v. Brown* (1908) 108 S. W. (Tex. Civ. App.) 421, esp. 437.

Directors possess authority to execute a lease of the corporate property, *Beveridge v. N. Y. Elevated R. Co.* (1889) 112 N. Y. 1, 19 N. E. 489, 2 L. R. A. 648; but see *Metropolitan & C. R. Co. v. Manhattan & C. R. Co.* (1884) 11 Daly (N. Y.) 373, at 468, 14 Abb. N. C. (N. Y.) 103; *Mercantile Library Hall Co. v. Pittsburg Library Assn.* (1896) 173 Pa. St. 30, 33 Atl. 744, ("Such an act is not in the management of the current affairs of the company, but is extraordinary and practically final"); to mortgage same, *Wood v. Whelen* (1879) 93 Ill. 153; but see *Matter of Wendler Mach. Co.* (1896) 2 App. Div. (N. Y.) 16, 37 N. Y. S. 444, 72 N. Y. St. 499, and *N. Y. Stock Corp. Law*, sec. 2; to compromise doubtful claims, *Stoeckle v. Hahn* (1895) 158 Ill. 79, 42 N. E. 150; to make an assignment for the general benefit of creditors, *Hutchinson v. Green* (1886) 91 Mo. 367, 1 S. W. 853 ("even against the expressed will of the stockholders"); *Rogers v. Pell* (1898) 154 N. Y. 518, 49 N. E. 75; *Goetz v. Knie* (1899) 103 Wis. 366, 79 N. W. 401.

Directors have no power to increase the capital stock, *Eidman v. Bowman* (1871) 58 Ill. 444; *Chicago City R. Co. v. Allerton* (1873) 18 Wall. (U. S.) 233, 21 L. ed. 902; to admit corporate insolvency and willingness to be adjudged bankrupt, *In re Quartz Gold Mining Co.* (1907) 157 Fed. 243; but see note, 8 Columbia Law Rev. 319; to release a subscription, *Hastings Lumber Co. v. Edwards* (1905) 188 Mass. 587, 75 N. E. 57; to accept a surrender of shares, *In re Beaconsfield Heights Estate Co.* (1896) 22 Vict. Law Rep. 97; to accept a fundamental amendment to the corporate charter, *Venner v. Atchison & C. R. Co.* (1886) 28 Fed. 581 (though vested with "all the corporate powers"); to assume a debt against a third person except in case of an urgent necessity, *Stark Bank v. United States Pottery Co.* (1861) 34 Vt. 144 (*sed qu.*).

See also, *Baker's Appeal* (1885) 109 Pa. St. 461, esp. pp. 471, 473.—Eds.

² Statement abridged. Opinion of Collins, M. R., omitted.—Eds.

Wilson the benefit of certain existing inventions in relation to the filtration, treatment, purification, storage, application, distribution, and use of liquids; and (k) to sell the undertaking of the company, or any part thereof, for such consideration as the company might deem fit, and in particular, for shares, debentures, or securities of any other company having objects altogether or in part similar to those of this company.

The articles provided as follows:—

"81. The company may by special resolution remove any director before the expiration of his period of office and appoint another qualified person in his stead. . . ."

"96. The management of the business and the control of the company shall be vested in the directors, who, in addition to the powers and authorities by these presents expressly conferred upon them, may exercise all such powers and do all such acts and things as may be exercised or done by the company, and are not hereby or by statute expressly directed or required to be exercised or done by the company in general meeting; but subject nevertheless to the provisions of the statutes and of these presents, and to such regulations, not being inconsistent with these presents, as may from time to time be made by extraordinary resolution, but no regulation shall invalidate any prior act of the directors which would have been valid if such regulation had not been made.

"97. Without prejudice to the general powers conferred by the last preceding clause, and to the other powers and authorities conferred as aforesaid, it is hereby expressly declared that the directors shall be entrusted with the following powers, namely, power—

"(1) To purchase or otherwise acquire for the company any property, letters patent, rights or privileges which the company is authorized to acquire, at such price, and generally on such terms and conditions, as they think fit; also to sell, lease, abandon, or otherwise deal with, any property, rights, or privileges to which the company may be entitled, on such terms and conditions as they may think fit."

"(16) To enter into all such negotiations and contracts and rescind and vary all such contracts, and execute and do all such acts, deeds, and things in the name or on behalf of the company as they might consider expedient for or in relation to any of the matters aforesaid, or otherwise for the purposes of the company."

The plaintiff A. H. McDiarmid, who was the holder of 1,202 shares in the plaintiff company, being desirous that the assets and undertaking of the plaintiff company should be sold, arranged terms on behalf of the company for the sale of them to a new company formed for the purpose of acquiring them, and had these terms embodied in a contract which was engrossed ready for execution by the company.

On January 2, 1906, a meeting of the shareholders of the company, convened by the directors in accordance with a requisition signed by the plaintiff McDiarmid and other shareholders in the company, was

held for the purpose of considering and if thought fit passing the following resolution:—

“That the company do sell the assets specified in the contract which has been produced to the meeting at the price and on the terms therein mentioned and contained and that the directors be and they are hereby directed to cause the common seal of the company to be affixed thereto within seven days and to carry the same into effect.”

The meeting was adjourned until January 16, when the resolution was passed by a majority of 304 votes, 1,502 votes for and 1,198 votes against it. Practically the whole of the 1,502 votes were given in respect of shares held by the plaintiff McDiarmid or his friends.

The directors, being of opinion that it would not be in the interests of the plaintiff company that the contract should be carried out, declined to comply with the resolution.

This was a motion by the plaintiff company and by the plaintiff McDiarmid, suing on behalf of himself and all other shareholders in the company, against the directors asking that the defendants might be ordered forthwith to affix the seal of the plaintiff company to the contract and to carry it into effect; that the defendants might be restrained by injunction until judgment or further order from dealing with or disposing of the assets of the plaintiff company intended to be comprised in the said agreement in any manner inconsistent with the terms thereof; and for the appointment of a receiver of the said assets.

The motion was heard before WARRINGTON, J., on February 23, 1906.

WARRINGTON, J., stated the facts, and continued:—The question I have to determine in this case is whether the shareholders of a company have power by a resolution passed by a simple majority of their number to order the directors to seal an agreement for the sale of the whole of the assets of the company notwithstanding that the directors may think that the sale is improvident, and that the terms on which it is to be carried out are not fit terms on which the company ought to carry out such a sale. To my mind this question depends upon the true construction of the articles. The only articles which are material are articles 96 and 97. (His Lordship read the articles, and continued:—)

The effect of this resolution, if acted upon, would be to compel the directors to sell the whole of the assets of the company, not on such terms and conditions as they think fit, but upon such terms and conditions as a simple majority of the shareholders think fit. But it does not rest there. Article 96 provides that the management of the business and control of the company are to be vested in the directors. Now that article, which is for the protection of a minority of the shareholders, can only be altered by a special resolution, that is to say, by a resolution passed by a three-fourths majority, at a meeting called for the purpose, and confirmed at a subsequent meeting. If

that provision could be revoked by a resolution of the shareholders passed by a simple majority, I can see no reason for the provision which is to be found in article 81 that the directors can only be removed by a special resolution. It seems to me that if a majority of the shareholders can, on a matter which is vested in the directors, overrule the discretion of the directors, there might just as well be no provision at all in the articles as to the removal of the directors by special resolution. Moreover, pressed to its logical conclusion, the result would be that when a majority of the shareholders disagree with the policy of the directors, though they cannot remove the directors except by special resolution, they might carry on the whole of the business of the company as they pleased, and thus, though not able to remove the directors, overrule every act which the board might otherwise do. It seems to me on the true construction of these articles that the management of the business and the control of the company are vested in the directors, and consequently that the control of the company as to any particular matter, or the management of any particular transaction or any particular part of the business of the company, can only be removed from the board by an alteration of the articles, such alteration, of course, requiring a special resolution.

No case has been cited to me which, in my opinion, has really any bearing on this question, which depends on the construction of the articles. In *Isle of Wight Ry. Co. v. Tahourdin* (1), which was a case under the Companies Clauses Consolidation Act, 1845, it was pointed out by the Court of Appeal that the resolution which it was proposed to submit to the meeting, and upon which the question arose, was one which could be carried by a simple majority of the company. Moreover, all that was there decided was that the court would not interfere to prevent a meeting of shareholders being held. No decision was given as to what would be the result with reference to the validity of any resolution which might be passed at the meeting.

On the whole, it seems to me that the resolution which was passed at the general meeting on January 16, 1906, is not one which the directors are bound to carry into effect. The consequence is, I must refuse the motion, with the usual result—that is to say, the costs will be the defendants' costs in the action.

From the above decision, plaintiffs appealed. * * * *

COZENS-HARDY, L. J.—* * * It is somewhat remarkable that in the year 1906 this interesting and important question of company law should for the first time arise for decision, and it is perhaps necessary to go back to the root principle which governs these cases under the Companies Act, 1862. It has been decided that the articles of association are a contract between the members of the company *inter se*. That was settled finally by the case of

Browne v. La Trinidad (1), if it was not settled before. We must therefore consider what is the relevant contract which these shareholders have entered into, and that contract, of course, is to be found in the memorandum and articles. I will not again read articles 96 and 97, but it seems to me that the shareholders have by their express contract mutually stipulated that their common affairs should be managed by certain directors to be appointed by the shareholders in the manner described by other articles, such directors being liable to be removed only by special resolution. If you once get a stipulation of that kind in a contract made between the parties, what right is there to interfere with the contract, apart, of course, from any misconduct on the part of the directors? There is no such misconduct in the present case. Is there any analogy which supports the case of the plaintiffs? I think not. It seems to me the analogy is all the other way. Take the case of an ordinary partnership. If in an ordinary partnership there is a stipulation in the partnership deed that the partnership business shall be managed by one of the partners, it would be plain that in the absence of misconduct, or in the absence of circumstances involving the total dissolution of the partnership, the majority of the partners would have no right to apply to the Court to restrain him or to interfere with the management of the partnership business. I would refer to what is said in *Lindley on Partnership*, 7th ed. p. 574: "Where, however the partner complained of has by agreement been constituted the active managing partner, the Court will not interfere with him unless a strong case be made out against him"—that is to say, unless there is some case of fraud or misconduct to justify the interference of the Court. Nor is this doctrine limited to a case of co-partners. It is not a peculiar incident of co-partnership: it applies equally to cases of co-ownership. I think in some of the earlier cases before Lord Eldon (1) with reference to the co-owners of one of the theatres, he laid down the principle that when the co-owners had appointed a particular member as manager the Court would not, except in the case of misconduct, interfere with him. And why? Because it is a fallacy to say that the relation is that of simple principal and agent. The person who is managing is managing for himself as well as for the others. It is not in the least a case where you have a master on the one side and a mere servant on the other. You are dealing here, as in the case of a partnership, with parties having individual rights as to which there are mutual stipulations for their common benefit, and when you once get that, it seems to me that there is no ground for saying that the mere majority can put an end to the express stipulations contained in the bargain which they have made. Still less can that be so when you find in the contract itself provisions which shew an intention that the powers conferred upon the directors can only be varied by extraordinary resolution, that is to say, by a three-fourths majority at one meeting, and that

(1) 37 Ch. D. 1.

(1) See *Waters v. Taylor*, (1808) 15 Ves. 10; (1813) 2 V. & B. 299.

the directors themselves when appointed shall only be removed by special resolution, that is to say, by three-fourths majority at one meeting and a simple majority at a confirmatory meeting. That being so, if you once get clear of the view that the directors are mere agents of the company, I cannot see anything in principle to justify the contention that the directors are bound to comply with the votes or the resolutions of a simple majority at an ordinary meeting of the shareholders. (I do not think it true to say that the directors are agents. I think it is more nearly true to say that they are in the position of managing partners appointed to fill that post by a mutual arrangement between all the shareholders.) So much for principle. On principle I agree entirely with what the Master of the Rolls has said, agreeing as he does with the conclusions of WARRINGTON, J.

When we come to the authorities there is, I think, nothing even approaching to an authority in favour of the appellants' case. *Isle of Wight Ry. Co. v. Tahourdin* (1) at the utmost contained a dictum which at first sight looked in favour of appellants; but, treating it as an authority, it was an authority upon an Act which differed in a vital point from the Act which we are now considering, because although by s. 90 of the Companies Clauses Act the directors have powers of management and superintendence very similar to those found in Table A, article 55, and in articles 96 and 97, that section contains these vital words: "And the exercise of all such powers shall be subject also to the control and regulation of any general meeting specially convened for the purpose." If those words had been found in the present Act of Parliament the appellants' case would have been comparatively clear. I see no ground for reading them into the Companies Act, 1862, or into the memorandum and articles of association of this company. For these reasons I think that the appeal must be dismissed.

GASHWILER v. WILLIS.

1867. 33 Cal. 11, 91 Am. Dec. 607.

APPEAL from the District Court, Fifth Judicial District, Tuolumne County.

The defendants were the stockholders of the corporation. The plaintiffs averred in their complaint that on or about the 23d day of September, 1865, they entered into negotiations with the corporation and with the stockholders for the purchase of a gold bearing quartz mine in Tuolumne County, known as the Rawhide Ranch Gold and Silver Mining Company's Claim, and that the defendants represented that they had full power to sell the same, subject only to a trust deed executed by the corporation to Danford N. Barney, of

(1) 25 Ch. D. 320.

the City of New York, in June, 1865, by which said Barney was authorized at any time between the first day of May and the first day of October, 1865, to sell the mine, according to certain written instructions referred to in the trust deed.

The plaintiffs further averred that the written instructions were not set forth in or attached to the trust deed, but that the defendants represented that by the instructions said Barney was required to sell the mine for the sum of fifty thousand dollars, to be paid to and received by the corporation and defendants in California before said first day of October, 1865, and in case payment was not made by that time the trust deed was to become null and void.

The complaint further averred that on the second day of October, 1865, the defendants represented that the sum of fifty thousand dollars had not been paid, and that they then had power to sell the mine, and that the plaintiffs on said last mentioned day bought the mine, and paid therefor the sum of twenty-five thousand dollars, took possession thereof, and expended money in erecting machinery on and improving it. That soon after doing so, plaintiffs discovered that the representations with regard to the written instructions requiring the fifty thousand dollars to be paid in California on or before the first day of October, 1865, were false, and that the instructions only required the money to be paid to said Barney in New York on or before said last named day, and that on the 27th day of September, 1865, said Barney had sold the mine to other parties in New York, and received the sum of fifty thousand dollars therefor, and that the plaintiffs, to avoid litigation, had been compelled, on the payment to them of the sum of fifty thousand dollars received by Barney, to convey and had conveyed the mine to the grantees of Barney. Plaintiffs averred that they had sustained twenty-five thousand dollars damages by the false representations of defendants, and asked judgment for that amount.

On the trial, as a part of their case, the plaintiffs offered in evidence the trust deed to Barney. The plaintiffs were nonsuited and appealed.

The other facts are stated in the opinion of the Court.

By the Court, SAWYER, J.:

The Rawhide Ranch Gold and Silver Mining Company is a corporation duly organized under the statutes of California, for the purpose of carrying on the business of mining. On the 29th of April, 1865, a special meeting of the stockholders of the corporation was held, pursuant to notice, at the office of the company, at which all the stockholders were present. At this meeting of the stockholders, all the stockholders being present and all the capital stock represented, a resolution was unanimously adopted authorizing S. S. Turner, T. N. Willis and James J. Hodges, Trustees of said corporation, for and on behalf of said corporation, to sell and convey to D. W. Barney the mine, mill, buildings, mining implements, and appurtenances belonging to said company. In pursuance of said resolution, and without any other authority shown, on the 5th of June following a

conveyance was executed by said Turner, Willis, and Hodges, Trustees, the commencement and form of execution of which are as follows :

"This indenture, made the 5th day of June, A. D. 1865, between the Rawhide Ranch Gold and Silver Mining Company, a corporation under the laws of the State of California, by S. S. Turner, T. N. Willis and James J. Hodges, Trustees of said corporation, who are duly authorized and empowered by resolution and order of said corporation to sell and convey," etc."

"In witness whereof we, as the Trustees of and for and on behalf of said corporation, have hereunto set our hands and seal (the said corporation having no seal) the day and year first above written.

"T. N. WILLIS, [L. S.]

"JAMES J. HODGES, [L. S.]

"S. S. TURNER, [L. S.]

"Trustees of the Rawhide Ranch Gold and Silver Mining Company."

On the trial, after proving the adoption of the resolution before referred to at a meeting of the stockholders, as stated, the plaintiffs offered said deed in evidence, and defendants objected to its introduction on the three grounds—that it did not appear to be the act or deed of the corporation; that it had not the signature of the corporation, and that it was not sealed with the corporate seal but with the individual seals of the Trustees. The Court sustained the objection and excluded the deed, to which ruling plaintiffs excepted; and this ruling presents the question to be determined. ?

Under the view we take, it will only be necessary to consider the first ground of the objection, and the question is does the instrument in question appear to be the act or deed of the corporation? If not, it was properly excluded, and the judgment must be affirmed. It is claimed by respondents that no authority is shown in the parties executing to execute the deed on behalf of the corporation. If the deed of a natural person, purporting to have been executed by an attorney in fact, were offered in evidence, it would, clearly, be inadmissible, without first showing the authority of the attorney. The recital of the authority in the deed itself would furnish no evidence whatever of its existence. The same is true of an artificial person—a corporation—at least, where the corporate seal is not affixed. Whether the rule would be different when the regularly adopted corporate seal is shown by competent proof to be affixed, it is not necessary now to inquire; for it affirmatively appears in this instance that the corporation has no seal, and that the parties executing the instrument used their respective private seals, no express authority to adopt such seals being shown. It may also be admitted for the purposes of this decision, that it is competent for the corporation to adopt the private seal of the several Trustees, or any of them, as its seal *pro hac vice*, and that the conferring upon the agent power to execute the

deed necessarily includes the power to adopt a seal on behalf of the corporation for the occasion. Still, as a seal regularly adopted by the corporation was not in fact used, it is necessary to show authority in the agent to execute the deed, in order to show, by implication, authority in him to adopt a seal for the occasion. The authority of the Trustees to execute the instrument in question must, therefore, affirmatively appear, or it does not appear to be the act or deed of the corporation.

We are not aware of anything in the law, independent of any authority expressly conferred by the corporation, which authorizes Turner, Willis and Hodges, in their official character as Trustees, to execute the instrument in question on behalf of the corporation. No law of the kind has been called to our attention, and we do not understand that any is claimed by appellants' counsel to exist. And there is nothing in the nature of those offices, as connected with the object and business of the company, from which a general power in the Trustees, when not acting as a Board, to sell and convey the mine, mill and other property of the company, could be implied. (*McCullough v. Moss*, 5 Den. 575.) The parties executing the instrument, then, if they had any authority in the premises, must have derived it from some corporate act; and the only act proved or relied on is the resolution adopted at the stockholders' meeting before mentioned. This was a meeting of the stockholders only. It was called as such, and the proceedings all appear to have been conducted as a stockholders' meeting. The resolution authorizing the sale and conveyance of the mine, etc., in question, was adopted by the stockholders, as such, at said meeting, and not by the Board of Trustees, or at any meeting of said Board. The Board of Trustees do not appear to have ever acted at all upon the matter in the character of a Board, but the testimony shows that they acted in pursuance of the said resolution adopted at the meeting of stockholders.

Section five of the Act authorizing the formation of corporations for mining purposes provides: "That the corporate powers of the corporation shall be exercised by a Board of not less than three Trustees, who shall be stockholders," etc. And section seven provides that: "A majority of the whole number of Trustees shall form a Board for the transaction of business, and every decision of a majority of the persons duly assembled as a Board shall be valid as a corporate act." (*Laws 1853*, p. 88, Sec. 5; 7 *Hittell's Gen. Laws*, Arts. 936, 938.) Conferring authority to sell and convey the corporate property is the exercise of a corporate power, and under these provisions the "corporate powers of the corporation" are to be exercised by the Board of Trustees when the majority are "duly assembled as a Board." When thus assembled and acting the decision of the majority "shall be valid as a corporate act." We find nothing in the Act authorizing the stockholders, either individually or collectively in a stockholders' meeting, to perform corporate acts of the character in question. The property in question was the property of the artificial being created by the statute. The whole title was in the corporation.

The stockholders were not in their individual capacities owners of the property as tenants in common, joint tenants, copartners or otherwise. (*Gorham v. Gilson*, 28 Cal. 484; *Mickles v. Rochester City Bank*, 11 Paige, 128.) This proposition is so plain that no citation of authorities is needed. Had the stockholders all executed a deed to the property, they could have conveyed no title, for the reason that it was not in them (*Wheelock v. Moulton et al.*, 15 Vt. 521); and what they could not do themselves they could not by resolution or otherwise authorize another to do for them. The corporation could only act—could only speak—through the medium prescribed by law, and that is its Board of Trustees. As well might the citizens of San Francisco in public meeting assembled, by unanimous resolution authorize certain Supervisors, designated by name, to sell and convey the City Hall. It is said, however, that the Trustees were also all present and participated in the proceedings at the stockholders' meeting and assented to the resolution; that the resolution therefore was approved by all of the constituents of the corporation, and the powers of the corporation were exhaustively exercised. But they were acting in their individual characters as stockholders, and not as a Board of Trustees. In this character they were not authorized to perform a corporate act of the kind in question. As well, also, might a valid ordinance be passed by the citizens of San Francisco in public meeting assembled, at which the Supervisors were all present and voted in the affirmative. Such an ordinance, when signed by the Mayor, would have the assent of all the constituents of the corporation as clearly as the resolution in question had in the present instance. But such is not the mode in which the corporation is authorized by the law of its creation to manifest its will and exercise its corporate powers. The power to sell and convey could only be conferred by the Trustees when assembled and acting as a Board. This is the mode prescribed. As a Board they could perform valid corporate acts, and confer authority within the province of their powers, upon the Trustees individually or upon any other parties to perform acts as the agents of the corporation. We are not without authorities upon this precise point.

In *Conro v. Port Henry Iron Company*, 12 Barb. 27, the same question arose. A lease of the company's iron works was made in pursuance of a resolution adopted at a meeting of the stockholders at which the Directors were present. It was held that the resolution imparted no authority to make the lease. The Court say: "The stockholders in this case had no power to make a lease or do any other administrative act in the management of the affairs of the corporation. If a lease could be made at all, it could be executed only in pursuance of the act of the Directors, who are the body appointed by the charter for the management of its affairs. It is no answer that the individual stockholders, who were present at the meeting when the lease was ordered, were also Directors. They did not meet as Directors, but as stockholders. The Mayor and Common Council of a municipal corporation can only act in the manner prescribed by

law. When not acting in their official character and in the mode prescribed by law, their acts are no more binding than those of other private citizens. (See, per Lord Mansfield, *Rex v. Head*, 4 Burr, 2,515, 2,521.)" (Ib. 63.)

McCullough v. Moss, 5 Den. 567, was an action upon a note purporting to have been executed by the Rossie Lead Mining Company. It was executed in pursuance of a resolution adopted by the stockholders. The statute of New York, conferring the power to manage the affairs of the corporation upon a Board of Directors, it will be seen, was similar to ours. Lott, Senator, in the Court for the Correction of Errors, said: "The affairs of the corporation were to be conducted by five Directors, a majority of whom formed a Board for the transaction of business, and a decision of a majority of those duly assembled as a Board was requisite to make a valid corporate act. (1 R. S. 600, Sec. 6.) The authority of the Board to the President and Secretary was therefore necessary to give validity to the note. This was not shown. The resolution passed at the meeting of the stockholders, contained in the letter of the Secretary, dated October 6th, 1839, could not bind the corporation, especially so as to affect the members not present. When a charter invests a Board with the power to manage the concerns of a corporation, the power is exclusive in its character. The corporators have no right to interfere with it, and Courts will not, even on a petition of a majority, compel the Board to do an act contrary to its judgment. (*Ang. & Ames on Corp.* 121-123, 151-164.) The stockholders, as such, in their collective capacity, could do no corporate act. The Directors were their representatives, and alone authorized to act. It is one of the fundamental conditions of the contract into which the corporators have entered by becoming members of the corporation, that its concerns shall be managed in the manner prescribed by the Act of incorporation, and from this no essential departure can be made." (Ib. 575.)

The same doctrine is held in *Cammeyer v. United German Lutheran Churches*, 2 Sandf. Ch. 208, 221, 228-9. The Vice Chancellor says: "The fact that a majority of the Trustees were present, acting as a Council, does not make the resolutions of the Council the act of the Board Trustees. Suppose, in the case of a bank, that at a general meeting of the stockholders certain resolutions should be adopted to sell land or do any other corporate act, and it should be made to appear that all the Directors of the bank were present and assenting to what was done, the corporation could not be bound unless the Directors, at a meeting of the Board, should concur in the resolutions. The Directors in the bank and the Trustees in this case are, by the charter, the select class or body which is to exercise the corporate functions. In order to exercise them they must meet as a Board, so that they may hear each other's views, deliberate, and then decide. Their separate action, individually, without consultation, although a majority in number should agree upon a certain act, would not be the act of the constituted body of men clothed with the

corporate powers. Nor would their action in a meeting of the whole body of corporators, or of another and larger class in which they are but a component part, be a valid corporate act. In thus acting they would not be distinguishable from their associates, and their action is united with that of others who have no proper or legal right to join with them in its exercise. All proper responsibility is lost. The result may be the same that it would have been if they had met separately, and it may be different. In the general assemblage influences may be brought to bear upon the Trustees which, in their proper Board, would be unheeded; and no one can say with certainty that their vote in the latter event would have been the same. It was held in the *Case of the Corporations*, (2 Coke, 476, by Fraser,) that where the power to make a by-law was in the Mayor and Aldermen, a by-law made by the Mayor, Aldermen, and Commonalty, was void." (Ib. 229.)

So also in *State v. Ancker*, 2 Rich. 245, the action of a Board illegally assembled was held to be without authority. The Court say: "Without being summoned together, the Board, as individuals, have no official authority, nor have they any original authority at all, either under the charter or the by-laws." (Ib. 281, 283.) The charter granted by Elizabeth to the borough of Helleston conferred the power of making by-laws on the Mayor and Aldermen, and the power of electing Burgesses on the Mayor, Aldermen, and Commonalty. A by-law was made by the Mayor, Aldermen, and Commonalty—the entire body. Its validity was in question in *Rex v. Head*, and it was held void on two grounds. One was, in the language of Lord Mansfield: "The body at large had no power to make by-laws, because the power is, by the charter, given to the Common Council, consisting of the Mayor, and Aldermen." (4 Burr, 2,521.) Yet the Mayor and Aldermen acted in connection with the Commonalty. These cases are in point, and none to the contrary have been called to our attention. They are the necessary consequence of the principles established by the great body of the authorities, that the corporate powers of corporations can only be exercised in the mode and through the instrumentalities prescribed by their charters. In this case, the resolution adopted by the stockholders was not a corporate act, and it conferred on the three Trustees named—whether they constituted the whole number of Trustees does not appear—no authority to perform a corporate act, to execute the deed, or adopt a seal for the occasion. It not only does not appear, then, that the instrument in question is the act or deed of the corporation, but it affirmatively appears that it was executed in pursuance of a resolution that conferred no authority whatever to perform a corporate act; for the plaintiffs themselves introduced in evidence the authority under which they claimed the act to have been performed, and upon which they relied. Having done this, we are not at liberty to indulge the presumption that the parties executing the deed on behalf of the corporation were otherwise duly authorized. The authority acted upon is affirmatively shown, and this fails. We think the deed properly

excluded. But even if it had been admitted without further proof of the authority of the parties to execute it, it would not have availed the plaintiffs. As there does not appear to have been any authority in the parties assuming to act, to sell or convey at all, it is unnecessary to discuss the other questions.

Judgment affirmed.

MR. JUSTICE RHODES did not express an opinion.

By the Court, SAWYER, J., on petition for rehearing:

The consequences assumed as the only basis of the argument in the petition for rehearing do not follow from anything determined or in any way suggested in the opinion in this case. We have nowhere held, or even intimated, that the board of trustees of a corporation can convey all the property of the corporation necessary to enable it to carry on the business for which it was organized, or do anything else destructive of the objects of its creation without the consent of its stockholders. We have not even held that it was competent for the trustees, acting as a board, to authorize the conveyance of the property now in question without the consent of the stockholders. There was no such question in the case. We simply held that the stockholders themselves could not authorize the trustees, acting as individual trustees, or anybody else, to convey it—that nobody could convey it unless authorized by some act of the board of trustees, acting as a board. It may be conceded for the purpose of this case that the board of trustees itself could not authorize a conveyance of the property in question without the consent of the stockholders, But it is unnecessary to consider that question, for the case does not present or even suggest it. It will be time enough to decide that question when it arises.

*Rehearing denied.**

* *Stoehlke v. Hahn* (1895) 158 Ill. 79, at 84, 42 N. E. 150; *McCullough v. Moss* (1846) 5 Denio (N. Y.) 567, at 575, *Accord.* But see *Spencer v. Lowe* (1912) 198 Fed. 961, and note, 13 Col. Law Rev. 257.

See *Lexington &c. Ins. Co. v. Page* (1856) 17 B. Mon. (Ky.) 412, esp. 439, 66 Am. Dec. 165; *Charlestown &c. Shoe Co. v. Dunsmore* (1880) 60 N. H. 85; *Loewenthal v. Rubber Reclaiming Co.* (1894) 52 N. J. Eq. 440, 22 Atl. 454/ ("In this connection it is worthy of remark that the stockholders, as such, have no power to make any contract or execute any work. Their power is confined to electing directors and advising them in their conduct of the business of the company," *per Pitney, V. C.*, at p. 445); *Moore v. Moore Mica Paint Co.* (1912) 135 N. Y. S. 210.

"The board of directors of a corporation do not stand in the same relation to the corporate body which a private agent holds toward his principal. In the strict relation of principal and agent, all the authority of the latter is derived by delegation from the former. * * * But in corporate bodies the powers of the board of directors are, in a very important sense, original and undelegated. The stockholders do not confer, nor can they revoke those powers. They are derivative only in the sense of being received from the state in the act of incorporation. The directors convened as a board are the primary possessors of all the powers which the charter confers, and like private principals they may delegate to agents of their own appointment the performance of any acts which they themselves can perform." *Comstock, J.*, in *Hoyt v. Thompson's Exr.* (1859) 19 N. Y. 207, at p. 216 (writ of error

GARMANY v. LAWTON.

1905. 124 Ga. 876, 53 S. E. 669.⁴

EQUITABLE petition. Before JUDGE CANN. Chatham Superior Court. June 30, 1905.

This case was by agreement tried before the presiding judge without a jury. He filed an opinion from which the following summary of facts is taken: "The Savannah District Messenger and Delivery Company was incorporated April 9, 1896, the capital stock being \$10,000, with the right to increase the capital stock to an amount not exceeding \$50,000, in the discretion of the board of directors. This is the only reference to a board of directors. The charter gives the right to mortgage the property of the corporation at any time. The original incorporators conveyed, by deed, the property and franchises of the corporation to C. H. Medlock and H. S. Jaudon on November 11, 1898. No certificates of stock had been issued at this time. There was never any stock issued to J. B. Floyd. On July 26, 1902, two certificates of stock were issued, one for fifty shares to H. S. Jaudon, the other for fifty shares to C. H. Medlock. Jaudon, Medlock and L. W. Walker were the directors. Walker never owned any stock. He was a nominal director. Walker moved away from Savannah, and no director was elected to fill his place. In July, 1899, Jaudon moved away from Savannah, and, until the time he sold out to Medlock all his interest in the company, he received reports from a bookkeeper concerning the business done by the company. After negotiating for two or three months, Jaudon agreed to sell out all his interest in the company to C. H. Medlock. The sale was consummated on May 8, 1903. On July 26, 1902, C. H. Medlock, to secure his individual indebtedness to I. D. LaRoche, made a deed, to secure a debt, to fifty shares of the capital stock of the Savannah District Messenger and Delivery Company. This was an individual transaction, and is not contended to be a corporate liability. On May 2, 1903, C. H. Medlock, as superintendent and manager, to secure the payment of a promissory note payable to the Citizens Bank of Savannah, due ninety days after date, for the sum of \$1,500, sold (conveyed) to John Lawton all the property, charter and franchises, good will, books, and accounts of the Savannah District Messenger and Delivery Company. This mortgage was signed, 'Savannah District Messenger and Delivery Company, by C. H. Medlock, Superintendent and Manager,' in the presence of three witnesses, one of whom was a notary public. The mortgage was not filed for record until September 26, 1904, and was recorded in the office of the clerk of the superior court of Chatham county on the

dismissed. 1 Black 518, [U. S.] 17 L. ed. 65). Approved and followed in *Beveridge v. New York &c. R. Co.* (1889) 112 N. Y. 1, at p. 23, 19 N. E. 489, 2 L. R. A. 648.—Eds.

⁴Portion of opinion omitted.—Eds.

same day. On September 24, 1904, C. H. Medlock suddenly died. On September 27, 1904, W. B. Stubbs was appointed and qualified as temporary administrator upon Medlock's estate, and conducted the business of the aforesaid corporation until October 6, 1904, when he presented a petition to the judge of the superior court of Chatham county asking for the appointment of a receiver to preserve and administer the assets of the corporation for the benefit of creditors. The judge signed the order before 10 o'clock A. M., October 6, 1904, appointing the receiver and restraining the said LaRoche and Lawton and Horace Rivers, as agent for Janie M. Garmany, their agents and attorneys, and the sheriff and his deputies, from interfering with said corporation, or its assets, in any way whatever, and from levying or attempting to levy any process thereon. Service of this order was acknowledged on October 6, 1904, by Adams & Adams, attorneys for said Lawton, and by Gordon & Elliott as attorneys for said Rivers, as agent. The legal evidence shows: There was no stock-book, there was no stock issued prior to that issued to C. H. Medlock and H. S. Jaudon, there was no minute-book kept, there was no corporate seal, and no record of any corporate action; from the time Jaudon and Medlock purchased the business Medlock conducted, as manager, all the business of the corporation; and this was especially true after Jaudon removed from Savannah, and entirely true after Medlock purchased Jaudon's stock in the corporation. The evidence shows that Rivers, as agent, and his attorneys knew of the contents of the mortgage to Lawton before he sued out his distress warrant. There is no evidence to show whether the levy of the distress warrant was made before or after the receiver actually took charge."

LUMPKIN, J.—(After stating the foregoing facts.) 1. A corporation is a legal entity, distinguished from any or all of its stockholders. That one person may own a majority or all of the stock of the corporation does not establish an identity between him and it, so as to make acts by him in his individual name its acts and binding on it. *Newton Manufacturing Co. v. White*, 42 Ga. 148; *Exchange Bank v. Macon Construction Co.*, 97 Ga. 1; *Spark v. Dunbar*, 102 Ga. 129; *Waycross Air-Line R. Co. v. Offerman R. Co.*, 109 Ga. 827. "When a corporation in a given matter is empowered to act only through its board of directors, or other select body of its officials, individual or separate action of the members of such board is not sufficient. The agent of the corporation is the board itself acting in its organized capacity, and not its members acting independently of its meetings." *Monroe Mercantile Co. v. Arnold*, 108 Ga. 449; *Branch v. Augusta Glass Works*, 95 Ga. 573; *England v. Dearborn*, 141 Mass. 590, 6 N. E. 837; *Mitchell v. Rome R. Co.*, 17 Ga. 574 (3). Agents must observe all the formalities required by the charter. *Dobbins v. Etowah Mfg. Co.*, 75 Ga. 243. The power of an agent to sign notes for his principal must be given in express terms or be necessarily implied from the nature of the agency actually created. *Exchange Bank v. Thrower*, 118 Ga. 435. In Maine a by-law providing for a regular meeting of a board of directors has been held merely direc-

tory. *Sampson v. Bowdoinham Steam Mill Corporation*, 36 Me. 78. While the rules above stated are correct as general rules, and an agent cannot bind a corporation by executing a mortgage on its property without its authority, unless it ratifies the act, yet the fact that the authority to make a chattel mortgage is not conferred by formal vote at a regular meeting will not in all cases render it void; especially where there has been a practice on the part of the company to transact business otherwise. 1 *Jones on Chat. Mges.* (4th ed.), § 51; *Ping. Chat. Mges.*, § 106; 1 *Cob. Chat. Mges.*, § 431; *Kraft v. Freeman etc. Pub. Asso.*, 87 N. Y. 625. Where a corporation loosely committed all its business affairs to a superintendent or general manager, and by a settled course of business he acted for it in all matters, including buying and selling property, and all of the directors and stockholders, with full knowledge of this, held no meetings and took no action, but acquiesced for a considerable length of time in his exercise of authority, if he borrowed money for the company and gave a chattel mortgage on its property, and no objection was made thereto, but his action was acquiesced in, authority to execute a mortgage might be inferred, or, if not original authority, ratification, as against the corporation or its stockholders who so acquiesced. See, on this subject, 10 *Cyc.* 1200; *Martin v. Niagara Falls Co.*, 44 *Hun* 131; *Estes v. German Bank*, 62 *Ark.* 7; *Sprangler v. Butterfield*, 6 *Col.* 356 (4); *Bank of Middlebury v. Rutland R. Co.*, 30 *Vt.* 160; *Wood v. Corry Waterworks Co.*, 44 *Fed.* 146, 12 *L. R. A.* 168; *Foot v. Rutland R. Co.*, 32 *Vt.* 633; *Longmont Supply Co. v. Coffman*, 11 *Col.* 551; *Poole v. West Point Asso.*, 30 *Fed.* 513. Some of these authorities are not in accord with the case of *Monroe Mercantile Co. v. Arnold*, *supra*, but they are cited to show the trend of adjudication in the direction of holding that while action on the part of directors or stockholders may not be performed in the regular and proper method, nevertheless where an officer is entrusted with the performance of the entire functions of the corporation, and this has become a settled policy, his act in executing a mortgage, acquiesced in by all the directors and stockholders, will be held binding. This is especially true in equity. Judge Thompson, in his article on "Corporations," in the *Cyclopedia of Law and Procedure*, says: "Where the shareholders of a corporation, by their direct act or acquiescence, invest the executive officers of the company with the powers and functions of the board of directors as a continuous and permanent arrangement, the board being entirely inactive, and the officers discharging all its duties, a mortgage on the property of the corporation, made and executed in its behalf by such officers, is valid, although not authorized by any vote of the shareholders or directors. . . . But in the absence of circumstances of assent and acquiescence such as may afford circumstantial or presumptive evidence of a precedent authorization, then, on principles already discussed, the directors can give a valid authorization of so important a measure as the mortgage of the property of the corporation, only when acting and consulting together as

a board, duly assembled." 10 Cyc. 1199; *Cunningham v. German Ins. Bank*, 101 Fed. 977 (3); *Palmer v. Toms*, 96 Wis. 367, 71 N. W. 654; *Miller v. Matthews*, 87 Md. 464, 40 Atl. 176. This affords a reconciliation between what might otherwise seem to be conflicting authority, the general rule being laid down in the latter part of the quotation, and the exceptional cases in the first part of it. In the present case the board of directors and the stockholders held no meetings and were entirely inactive, devolving the whole management of the affairs of the company upon Medlock. And this was not a casual or occasional state of affairs, but was continuous and permanent. Medlock was negotiating with Jaudon, the president, for his stock, and took a formal transfer of it shortly after the mortgage was executed. LaRoche, who held the stock issued to Medlock as security, is not complaining. And as one witness expressed it, Medlock was "the lock, stock and barrel of the concern,—he was the whole thing." Or, as another witness expressed it, "he practically did all the running." Apparently he had exercised the entire functions of the corporation, including buying and selling property. After his purchase of Jaudon's stock, he renewed the note in the name of the corporation more than once. Under this condition of affairs we think that the mortgage should be held good as against the corporation, and also as against a subsequent creditor who obtained a lien, if at all, by suing out a distress warrant after the record of the mortgage and with full knowledge of such mortgage. The rent accrued long after the making of the mortgage. Indeed the landlord's lien arose only upon the levy of the distress warrant. Civil Code, § 3125. And the evidence leaves it in doubt as to when the levy was made, relatively to the time when the restraining order was passed. The judge of the superior court did not err in holding that the lien of the mortgage was superior to that of the distress warrant. See 10 Cyc. 1196; *Antietam Paper Co. v. Chronicle Pub. Co.*, 115 N. C. 143, 20 S. E. 366. * * *

Judgment affirmed. All concur.^a

^a"The proof was ample to show that the corporation of Scanlan & Co. practically devolved the powers of the board of directors upon its executive officers, and that this method of doing business was not casual and temporary merely, but continuous from the date of its commencing to do business to the end. The board of directors was dormant. [The rule is that where, by the direction or acquiescence of the stockholders, the executive officers of a corporation assume and exercise the functions of the board of directors, the corporation and those deriving rights from it while it is so managing its affairs are bound by the acts of its officers to the same extent as if they had been directed by the board.] In so far as the duties of the directors are not expressly prescribed by the charter, they derive their powers from the stockholders, who may, if they see fit, select other agencies for the transaction of the corporate business." Severens, J., in *Cunningham v. German Ins. Bank* (1900) 101 Fed. 977, at p. 980, 11 C. C. A. 609, *Accord*.

See also, *Smith v. Wells Mfg. Co.* (1897) 148 Ind. 333, 46 N. E. 1000; *Sherman v. Fitch* (1867) 98 Mass. 59; *Manhattan Brass Co. v. Webster & Queensware Co.* (1889) 37 Mo. App. 145 (conveyance authorized at meeting of all the stockholders upheld); *Chicago & C. R. Co. v. Union Pac. R. Co.*

PEOPLE EX REL. MANICE v. POWELL.

1911. 201 N. Y. 194, 94 N. E. 634.

APPEAL from an order of the Appellate Division of the Supreme Court in the first judicial department, entered October 28, 1910, which affirmed, as matter of law and not in discretion, an order of Special Term denying a motion for a peremptory writ of mandamus to compel the defendants to reinstate the relator as a director of the respondent Atlantic Terra Cotta Company.

The facts, so far as material, are stated in the opinion.

CHASE, J.—The relator, who had been elected a director of the defendant Atlantic Terra Cotta Company for a term which will not expire until January, 1912, has been removed from his office as a director as hereinafter stated, and another person has been elected to fill the alleged vacancy, and he is now performing the duties as such director. The relator seeks by peremptory mandamus to set aside the proceedings by which it is alleged he was removed and to be reinstated in his office as a director.

The defendant Atlantic Terra Cotta Company is a domestic corporation organized in February, 1907, for the purpose of manufacturing and selling architectural terra cotta. Its certificate of incorporation provides for a board of three directors. Soon after the company was organized the number of directors was increased from three to twelve by unanimous consent of the stockholders, and the by-laws were amended to provide for a division of the directors into three classes of four directors each, and directors were thereafter elected for such terms respectively so that the term of office of four of such directors would expire each year. In January, 1909, the board of directors changed the general officers of the corporation by electing a new president, secretary and treasurer, general superintendent and general counsel. The relator was opposed to such changes, and it is alleged that he and those deposed from said offices were thereafter hostile to the new management.

Early in January, 1910, an amended certificate of incorporation, altering the original certificate of incorporation of the defendant corporation, was filed, by which there was included therein the following provision: "If the notice of any regular or special meeting of the board of directors shall contain a statement to the effect that the board will at such meeting consider whether sufficient cause exists for the removal of some specified person from the office of director of the corporation, and if the board, after consideration of such question, shall determine at such meeting by the affirmative vote of two-

(1891), 47 Fed. 15 ("In this, as in any other stock corporation, with the stockholders rests not only the ownership of the property, but the ultimate and absolute power and control," *per* Brewer, J., at p. 19), *affd.* (1895) 51 Fed. 309, 2 C. C. A. 174, and 163 U. S. 564, esp. (595-600), 16 Sup. Ct. 1173, 41 L. ed. 265.)—Eds.

subsequent statement
Reserved to
S.H.

thirds of all the directors in office that sufficient cause exists for the removal of such person from such office, and that his removal is desirable and for the best interests of the corporation, and if such determination shall thereafter be approved and ratified at a duly called stockholders' meeting by the affirmative vote of the holders of two-thirds of the outstanding stock of the corporation, then such person shall immediately cease to be a director of the corporation, and the resulting vacancy in the board of directors shall be filled as provided in the by-laws."

Such alteration of the certificate of incorporation had been opposed by the relator, but it was authorized by a majority vote of the directors at a meeting held December 30, 1909, and by a vote of stockholders representing more than three-fifths of the capital stock at a meeting of stockholders called for that purpose and held December 24, 1909.

The annual meeting of the stockholders was called to be held January 21, 1910, and also a special meeting of the stockholders to be held January 19 for the purpose of reducing the number of directors of the company from twelve to six.

Before the meeting was held on January 19 a stockholder of the company brought an action to prevent such meeting being held upon the ground that a reduction in the number of the board of directors violated certain alleged contract rights specified in the complaint in that action. A temporary injunction was obtained. An appeal was taken to the appellate division from the order granting such temporary injunction, and the order was reversed and the motion denied. (*Bond v. Atlantic Terra Cotta Co.*, 137 App. Div. 671.) The annual meeting of stockholders was adjourned from time to time until May 18, and the special meeting of the stockholders for the purpose of reducing the number of directors was adjourned from time to time until April 26. On April 26 the order granting an injunction having been reversed and the motion having been denied, the special meeting of stockholders was held and the number of directors was reduced from twelve to six.

On May 7 a special meeting of the directors of the company was called for May 11, and included in the notice of such meeting was the following: "The board will at this meeting consider whether sufficient cause exists for the removal of William Manice from the office of director of the company." The meeting was, at the request of counsel for Manice, adjourned until the same hour on May 12.

At the meeting on May 12 the relator with his counsel and all the directors except one, and the general counsel of the corporation were present, and a resolution was offered of which the following is a copy: "Whereas, William Manice has participated in the organization of the Federal Terra Cotta Company, a competitor of this company, and is now an officer and director of and otherwise interested in said company; and,

"Whereas, The conduct of said Manice has not in the judgment of this board been for the best interests of this company;

"Resolved and determined, That sufficient cause exists for the removal of said Manice from the office of director of this company and that his removal from such office is desirable and for the best interests of this company."

Counsel for the relator objected to the consideration of the resolution upon the ground that the amendment to the certificate of incorporation providing for removal of directors did not apply to the relator, because he was a member of the board at the time it was passed and his term of office had not yet expired, and upon the ground that there was no by-law authorizing the procedure. Counsel for the corporation suggested that the objection be put in the form of a motion, and it was so offered as a resolution and defeated by a vote of eight to three. Counsel for the relator then asked that inasmuch as the relator had then for the first time been apprised of the charges implied in the resolution, he should be allowed a reasonable time within which to confer with counsel and determine what answer to make to such charges. The chairman of the meeting asked relator's counsel what he considered a reasonable time, and suggested that the directors might be willing to allow him ten or fifteen minutes. Counsel for the relator replied that he meant by a reasonable time until Monday, May 16, 1910, which would mean four days. A motion was then made that the relator be granted a reasonable time, to wit, until Monday, May 16, to confer with counsel and determine what answer to make to such charges, but it was defeated. The resolution to remove Manice from the office of director was then carried. The meeting did not occupy more than five or ten minutes.

At the stockholders' meeting held May 18 four of the directors, two of those whose terms of office would expire in 1911, and two of those whose terms of office would expire in 1912, resigned, and but two were elected to take the place of those whose terms of office expired in 1910. The board then consisted of six directors, of whom, except for the removal that we have mentioned, the relator was one of the class whose term of office would expire in 1912. At such stockholders' meeting a resolution was offered that all of the acts of the board of directors, including the determination of the board of directors that sufficient cause exists for the removal of William Manice from the office of director of the company and that his removal is desirable and for the best interests of the company, be approved and ratified. A resolution was then offered as follows:

"Whereas, The amendment of the certificate of incorporation adopted on or about the 24th December, 1909, which provided that the directors shall 'consider' whether sufficient cause exists to remove a director and that if the board after such 'consideration' shall 'determine' that cause exists, contemplates the furnishing to the person charged with a copy of the charge made against him and giving him an opportunity to confer with counsel and a reasonable time to reply thereto and be heard in his own defense; and,

"Whereas, in the case of Mr. Taylor and Mr. Manice neither of them have been furnished with a copy of the charge made against him and neither of them have ever been given an opportunity to reply thereto or to be heard before the board of directors in his own behalf;

"Resolved, That under the by-laws there has as yet been no proper or legal determination that a cause for the removal of either Mr. Taylor or Mr. Manice exists and that, therefore, under the by-laws the question as to the removal of either Mr. Taylor or Mr. Manice is not now properly before this meeting."

Such resolution was defeated. The counsel for the relator then asked that he be furnished with a copy of the charges made against relator, and he was told by the chairman of the meeting that the charges were incorporated in the resolution adopted at the meeting of the board of directors. A motion was then made to adjourn, which was defeated. The resolution approving and ratifying the acts of the board of directors was then adopted by a vote of stockholders holding more than two-thirds of all the stock of the corporation. A meeting of the directors was held immediately after the adjournment of the stockholders' meeting on May 18, and a director was elected to fill the vacancy caused by the removal of the relator, and he is now acting as such director by alleged right of such election. The relator claims that his alleged removal is wholly illegal and void.

The learned justice at Special Term, in denying the motion for a peremptory mandamus, referring to the relator, said: "As a director he was but an agent of the corporation, and the principles of the law of agency were applicable to him. If wrongfully removed before the expiration of the period for which he was elected, he is entitled to recover if damages have resulted; but he cannot insist upon being retained in a fiduciary relation toward the stockholders against the latter's wishes. The stockholders had the power to revoke the agency, though not the right."

In the reason so given for the denial of the motion we think the distinction between a person occupying an ordinary contract relation as an agent for a principal and a person elected for a specified term as a director of a private corporation was wholly overlooked.

"The board of directors of a corporation do not stand in the same relation to the corporate body which a private agent holds toward his principal * * *. In corporate bodies the powers of the board of directors are, in a very important sense, original and undelegated." (Hoyt v. Thompson's Executors, 19 N. Y. 207, 216; Beveridge v. N. Y. E. R. R. Co., 112 N. Y. 1, 22, 23.)

While the ordinary rules of law relating to an agent are applicable in considering the acts of a board of directors in behalf of a corporation when dealing with third persons, the individual directors making up the board are not mere employees, but a part of an elected body of officers constituting the executive agents of the corporation. They hold such office charged with the duty to act for the corpora-

tion according to their best judgment, and in so doing they cannot be controlled in the reasonable exercise and performance of such duty. As a general rule the stockholders cannot act in relation to the ordinary business of the corporation, nor can they control the directors in the exercise of the judgment vested in them by virtue of their office.

The relation of the directors to the stockholders is essentially that of trustee and *cestui que trust*. The peculiar relation that they bear to the corporation and the owners of its stock grows out of the inability of the corporation to act except through such managing officers and agents. The corporation is the owner of the property, but the directors in the performance of their duty possess it, and act in every way as if they owned it.

This court, in *Bosworth v. Allen* (168 N. Y. 157), referring to directors, say: "While not technically trustees, for the title of the corporate property was in the corporation itself, they were charged with the duties and subject to the liabilities of trustees. Clothed with the power of controlling the property and managing the affairs of the corporation, without let or hindrance, as to third persons they were its agents, but as to the corporation, itself, equity holds them liable as trustees. (2 Pomeroy's Equity Jurisprudence, secs. 1061, 1063, 1088, 1097.)"

The relator occupied a position toward the corporation that was one of trust and responsibility. He was given power and authority to act not only substantially uncontrolled by the corporation, but he was not subject to discharge as an employee unless such right is vested in some court or body of persons by statute or in its articles of incorporation duly authorized by statute.

It would be somewhat startling to the business world if we definitely announced that the directors of a corporation were mere employees and that the stockholders of the corporation have the power to convene from time to time and remove at will any or all of the directors, although their respective terms of office have not expired.

It is and was prior to the amendment of said certificate of incorporation provided by statute that an action may be maintained against a director of a corporation to procure a judgment suspending him from exercising his office if it appear that he has abused his trust or to remove him from office upon proof or conviction of misconduct. (General Corporation law, sections 90 and 91; former sections 1781 and 1782 of the Code of Civil Procedure.) It is provided by section 307 of said General Corporation Law that a director shall not be suspended or removed from office by a court or judge otherwise than by the final judgment of a competent court in an action brought by the attorney-general as prescribed by said section 90 of that act. Statute
→

The statute providing for an action in the name of the attorney-general to suspend or remove a director is not exclusive of such reasonable and lawful charter provision relating thereto as may be included in the articles of incorporation. Without some statute or provision of the charter authorizing his removal or suspension, a

director cannot be removed or suspended from office until the end of his term, at least without cause] (Thompson on Corporations [2nd ed.] secs. 1084, 1085, 1086; Taylor on Corporations, sec. 649; Cook on Corporations, sec. 711; Morawetz on Private Corporations, secs. 541, 542.)

Upon the merits of the controversy presented by this appeal there are two important questions for consideration: 1. Whether the amendment of the certificate of incorporation contemplates the removal of a person as a director without a reasonable notice of the alleged sufficient cause for his removal and a reasonable opportunity for him to be heard upon the question whether his removal is desirable and for the best interests of the corporation.

2. Whether the relator had a reasonable notice of the alleged sufficient causes for his removal and a reasonable opportunity to be heard before the board of directors in relation thereto.

We shall not further discuss the merits of the relator's claim because we are of the opinion that his remedy, if any, is not by mandamus. * * *

The action in the nature of a quo warranto affords a complete remedy to the relator if he is legally entitled to be reinstated and renders the proceeding by mandamus not only unnecessary but contrary to the recognized practice of the courts.

The special term and the appellate division were right, therefore, as a matter of law in refusing the writ, and the order should be affirmed, with costs.

CULLEN, Ch. J., HAIGHT, VANN, WILLARD BARTLETT, HISCOCK and COLLIN, JJ., concur.

*Order affirmed.*⁶

Section 2.—Rights.

A—COMPENSATION.

CHEENEY v. LAFAYETTE ETC. R. CO.

1873. 68 Ill. 570.

APPEAL from the Circuit Court of Livingston county; the Hon. CHARLES H. WOOD, Judge, presiding.

This was an action of assumpsit, by Jonathan H. Cheeney against the Lafayette, Bloomington and Mississippi Railway Company, to recover for services, as stated in the opinion.

⁶In *Gold Bluff &c. Corporation v. Whitlock* (1903) 75 Conn. 669, 55 Atl. 175, held that the stockholders may amend the by-laws so as to increase the number of directors.

See *Isle of Wight R. Co. v. Tahourdin* (1884) L. R. 25 Ch. Div. 320, 332 ("I am of opinion that under sec. 91 a general meeting of shareholders has

MR. JUSTICE WALKER delivered the opinion of the court:

The Lafayette, Bloomington and Mississippi Railroad Company was organized, and appellant was elected a director. In January, 1870, the company, through its board of directors, created an executive committee, consisting of five persons, who, with the chief engineer, were empowered to make contracts and provide funds for the construction and equipment of the road; and, in the month of January, 1870, appellant was appointed a member of the executive committee, and continued to act as such until the last of January, 1872. This service is claimed by appellant to have been worth \$1,000.

He was, also, in September, 1869, appointed as agent of the company to procure the right of way through McLean county, and he rendered services in that capacity for which he claims \$600. He was also appointed, in the autumn of 1872, an agent to solicit and procure subscriptions to aid in constructing the road, and he claims he devoted two months of his time to that service, and that it is worth \$400; that whilst a member of the executive committee, he made frequent trips to Chicago and Lafayette on the business of the company; that in the spring of 1871, after the road-bed was graded and bridged, he was appointed as a member of a special committee to go East to make, if possible, a contract for the completion of the road, and he went to Philadelphia and New York, and was absent two weeks, and afterwards conferred with other parties with a view of contracting for the completion of the road, and in doing so went to Chicago, Lafayette, Cleveland and New York, and was absent four weeks.

It appears that the claim for these services was presented to the company and audited by its executive committee on the 13th day of January, 1872, amounting to \$4,000; that a warrant for that amount was drawn on the treasurer; that the board of directors, at a meeting on the 31st day of January, 1872, appropriated \$25,000 to pay this and other claims, but appellant testifies that he has never received any part of his claim, and brought his action of assumpsit to recover for work and labor and for money paid out for the use of the company.

A warrant of attorney was given by the company to confess a judgment, which was entered. But subsequently a motion was made

power to remove directors"); *Ward v. Davidson* (1886) 89 Mo. 445, 463, 1 S. W. 846 (court may remove directors for misconduct).

As to qualifications of directors and de facto directors, see *Matter of Ringler & Co.* (1912) 204 N. Y. 30, 97 N. E. 593; cf. *Waterman v. Chicago & C. R. Co.* (1892) 139 Ill. 658, 29 N. E. 689, 15 L. R. A. 418, 32 Am. St. 228.

As to delegation of directors' powers, see *Gillis v. Bailey* (1850) 21 N. H. 149, 160-5. Cf. *Hoyt v. Thompson's Exr.* (1859) 19 N. Y. 207 (writ of error dismissed, 1 Black [U. S.] 518, 17 L. ed. 65); *Sheridan Elec. Light Co. v. Chatham Nat. Bank* (1891) 127 N. Y. 517, 28 N. E. 467 (directors may invest an executive committee "with power to transact the business of the company during the interval between the meetings of the board of trustees"). See also, *Chicago Hansom Cab Co. v. Yerkes* (1892) 141 Ill. 320, 30 N. E. 667, 33 Am. St. 315.—Eds.

to set aside this judgment, which was done, and the company let in to plead. After filing pleas, the case was submitted to the court for trial, without a jury, by consent of parties. The court found for the defendant, and entered a judgment in bar of the recovery, and for costs, and plaintiff brings the record to this court on appeal.

In adopting the by-laws of the company, no salary or provision for compensation of the officers was made, but it is claimed they all understood and expected that a reasonable compensation would be made for their services rendered in the discharge of their duties.

The doctrine is stated in *Redfield on Railways*, 406, that, in England, to entitle directors, etc., to receive compensation, it must be provided for and fixed by the by-laws of the organization, and that the doctrine in this country requires such compensation to be thus fixed, or at least by a resolution of the directors spread on the minutes of their proceedings, and we apprehend that compensation, whether the one mode or the other be adopted, must be fixed before the services are rendered.

In the case of the *Am. Cent. R. R. Co. v. Miles*, 52 Ill. 174, it was held that a director could not recover compensation for services unless they were thus fixed by the directors, and the services of the president and other officers of the company fall fully within the principle of the rule. The president and directors of such a company are trustees for the stockholders, and it is for that reason that the law does not imply a promise to pay them for discharging the duties imposed upon persons occupying that relation.

At the common law, a trustee was not entitled to compensation, and could not recover on a *quantum meruit*. And it was in the application of this rule that it was held, in *The Loan Association v. Stonemetz*, 39 Pa. 534, that a resolution passed by the corporation after services were rendered, that the officer be paid a sum of money for services as chairman of a committee, was without consideration, and imposed no obligation on the corporation that could be enforced. And the case of *N. Y. and N. H. R. R. Co. v. Ketcham*, 27 Conn. 170, illustrates the rules in holding that it does not matter that the services were rendered in the expectation and understanding that the officer should be paid. And in the case of *Butts v. Wood*, 37 N. Y. 317, it was held, notwithstanding the bill for services rendered by an officer where no by-law or resolution had fixed his pay, and the bill was allowed by the board, that, "one holding a position of trust cannot use it to promote his individual interest in any manner in disposing of the trust property; that the circumstances under which the bill was allowed was a fraud on the shareholders, and to permit such a transaction to stand, would be a reproach to the administration of justice."

In the *N. Y. and N. H. R. R. v. Ketcham*, 27 Conn. 175, the court use this language: "It would be a sad spectacle to see the managers of any corporation assembling together and parceling out among themselves the obligations and other property of the corporation in payment for past services."

In the case of *Dustin v. The Imperial Gas Co.*, 3 Barn. & Adol. 125, it was held that, whilst agents and employees might, perhaps, recover for services rendered for a corporation, a director could not, unless provision therefor had been made by resolution having the force of a by-law, or by such a by-law. And it was said that such officers differ materially from mere agents and employees; that directors are managers or governors, and not agents.

No person is under the slightest compulsion to accept the position, and if he is unwilling to do so without compensation, public policy requires that his compensation should be fixed and certain before he enters upon the discharge of the duties of his office. This rule must apply to services rendered by persons holding the office of directors, who have the control of the funds of the body. But a person, not a director and having no control over the funds and property of the corporation, rendering services, does not occupy the relation of trustee to the company, and does not fall within the rule, and may recover a reasonable compensation for services rendered. The law has never conferred on trustees the authority to profit by the exercise of the powers and duties of their position.

This, then, disposes of the claim of appellant for services rendered as a director of the company. But the question arises, whether or not he rendered services for the company which do not pertain to his duty as director, and if so, whether he may recover a fair compensation for such service.

It is said by Lord Coke, in his Commentaries on Littleton, 66 b, that "a corporation aggregate of many cannot appear in person, for, albeit the bodies natural whereupon the body politic consist may be seen, yet the body politic or the corporation itself cannot be seen, nor do any act, but by attorney." And in *Angell & Ames on Corp.*, p. 210, it is said that, "in general, the only mode in which a corporation aggregate can act or contract, is through the intervention of agents, either specially designated by the act of incorporation or appointed and authorized by the corporation in pursuance of it." And it was held, in *Waller v. Bank of Ky.*, 3 J. J. Marsh 206, that the agents of a corporation, like the agents of natural persons, are entitled to recover compensation according to what it is reasonably worth. In that case the law required the body to appoint a clerk, but neither the law nor any by-law or resolution of the board of directors fixed his compensation, and he was permitted to recover in assumpsit. See *Hall v. The Vt. and Mass. R. R. Co.*, 26 Vt. 401.

If, then, appellant was appointed to act as agent for the performance of duties outside of those devolving on him as director, it is but reasonable and just that he should be allowed to recover a fair compensation for such services. *Shackleford v. N. O., J. and G. N. R. R. Co.*, 37 Miss. 202.

Because he was a member of the board of directors, it does not follow that he was bound to perform any and all duties usually exercised by agents properly appointed, and when he performed such duties under an appointment by a resolution of the board, he should

Our Case.

be allowed compensation therefor.] Where an attorney is employed to attend to the general or special affairs of the company, he should be compensated. So of a secretary or clerk, and an agent to solicit subscriptions and to procure the right of way, etc.

It would, then, follow that, as appellant was appointed to solicit subscriptions of stock, and to procure the right of way for the road, he may recover, unless that duty was imposed on him as a director by the charter or the by-laws. In performing those duties, it is more than probable that he acted as an agent, and, not as a director, and should be permitted to recover for such extra service, but if this duty was imposed by the charter or the by-laws of the company as a director, then a recovery could not be had therefor. The duties he performed as a member of the executive committee in making efforts to contract for the construction of the road, including time and travel, were a part of his duty as a director, and, from the authorities above referred to, he has no right to recover for them. Nor is it an answer to say, that the company could have entrusted the duties of the executive committee to others not directors or even stockholders, and paid them a fair compensation for their time and skill. They had the power to so act as directors, and they, as directors, or as a part of them, performed the services.

The judgment of the circuit court must be reversed and the cause remanded.

*Judgment reversed.*¹

B—INDEMNITY.

IN RE NATIONAL FINANCIAL CO.

1868. L. R. 3 Ch. App. Cas. 791.²

THIS was an appeal from an order made by Vice-Chancellor Stuart at Chambers.

The National Financial Company, Limited, being, by its articles of association, authorized to hold shares in other companies, agreed

¹ *Ellis v. Ward* (1890) 137 Ill. 509, 25 N. E. 530; *Bagley v. Carthage &c. R. Co.* (1900) 165 N. Y. 179, 58 N. E. 895; *National Loan & Investment Co. v. Rockland Co.* (1899) 94 Fed. 335, 36 C. C. A. 370, *Accord.* Cf. *Bassett v. Fairchild* (1901) 132 Cal. 637, 64 Pac. 1082, 52 L. R. A. 611.

See also *Fitzgerald &c. Const. Co. v. Fitzgerald* (1890) 137 U. S. 98, 34 L. ed. 608, 11 Sup. Ct. 36; *Montana Tonopah Min. Co. v. Dunlap* (1912) 196 Fed. 612.

In *Lowe v. Ring* (1904) 123 Wis. 370, 101 N. W. 698, held that the rule as to compensation of directors applies likewise to the president and other principal officers of a corporation, who are also stockholders or directors, so far as it concerns their regular and usual duties. See, to similar effect, *Sears v. Kings County &c. R. Co.* (1890) 152 Mass. 151, 25 N. E. 98, 9 L. R. A. 117.—Eds.

² Concurring opinion of Selwyn, L. J., omitted.—Eds.

to take a number of shares in the Tyne Iron Ship-building Company, Limited. These shares were to be allotted to nominees of the National Company, and those nominees were to hold the shares when allotted on trust for the National Company. In pursuance of this arrangement, 100 shares in the Tyne Company were allotted to Mr. George Maitland, one of the directors of the National Company, and he was registered as the owner of those shares. He executed a declaration of trust of the shares for the National Company, and also blank transfers. In April, 1865, an arrangement was made for the amalgamation of the National Company with a company called the Oriental Commercial Bank, Limited, and all the assets of the former company were handed over to the latter company. At this time Maitland executed a transfer of the 100 shares in the Tyne Company to two directors of the bank, as nominees of the bank, [but this transfer was never registered in the books of the Tyne Company]. Orders were afterwards made for the compulsory winding up of both the National Company and the bank, and an order was made giving liberty to the official liquidator of the bank to attend the proceedings in the liquidation of the National Company. The Tyne Company went into a voluntary liquidation, and calls to the amount of 3250L. were made upon Maitland in respect of the 100 shares, no part of which sum he paid. On the 28th of April, 1868, the vice-chancellor, upon the application of Maitland, made the following order: "The judge being of opinion that the said George Maitland is entitled to be indemnified by the National Financial Company in respect of and against the calls, amounting to 3250L., that have been made on the said George Maitland by the liquidators of the Tyne Iron Ship-building Company in respect of 100 shares held by the said George Maitland as the nominee of and trustee for the National Financial Company, and in respect of the interest due on the said calls, and in respect of all future calls that may be duly made and payable by the said George Maitland in respect of the said shares, and all interest on the same; it is ordered that the said George Maitland is entitled to rank as a creditor of the National Financial Company for the said sum of 3250L. and interest, and for any such future calls and interest on the same, and for his costs as hereinafter mentioned, the said George Maitland undertaking that the official liquidator of the National Financial Company be at liberty to pay over to the liquidators of the Tyne Iron Ship-building Company the dividends which may become payable from time to time in the liquidation of the National Financial Company to the said George Maitland, or the liquidators of the Tyne Iron Ship-building Company, in respect of the said sum of 3250L. and interest, and any future calls that may be made upon him as aforesaid; the liquidators of the Tyne Iron Ship-building Company consenting to be bound by the terms of this order, and to accept whatever moneys may be so paid or payable by the official liquidator of the National Financial Company, in full satisfaction of all claims by the Tyne Iron Ship-building Company, or the liquidators thereof, against the said George Maitland, or his

estate, in respect of the said 100 shares; and it is ordered that the costs of the said George Maitland of and incident to this application, including his costs, charges, and expenses properly incurred as such nominee as aforesaid, be taxed as between solicitor and client, and the said George Maitland is to be at liberty to add the amount thereof to his aforesaid debt." From this order the official liquidator of the Oriental Commercial Bank appealed.

SIR W. PAGE WOOD, L. J.—

It does not appear to me that the Vice-Chancellor's order does anything more than work out the most common and ordinary justice. As between Mr. Maitland and the Tyne Company, according to my view in Hoare's Case, 2 J. & H. 229, to which I adhere, I am of opinion that Mr. Maitland is the shareholder. If the Tyne Company choose to do so, I do not see anything to prevent their exacting from him all payments to which as a shareholder he is liable. [But, as between Mr. Maitland and the National Financial Company, the latter are the shareholders, they are simply his cestuis que trust, and his name has been used for their accommodation and for their convenience.] The position of a trustee so situated is not that he is to wait till he is thrown into prison in consequence of his cestuis que trust not paying what it is their bounden duty to pay; he has a right to say, "Provide me with the funds which are necessary to meet this difficulty; these are not my shares; I am not the owner of them; I have nothing to do with them; they are yours." Maitland being the trustee, and having been called upon to pay the 3250L., as between him and the cestuis que trust, the latter ought to find the money to pay it. He is called upon to make the payment, and he is entitled to rank as a creditor of the National Company for this sum and for any future claim, he undertaking not to pocket this money, but to hand it over in discharge of the liability against which he is entitled to be indemnified. He has therefore undertaken that the official liquidator of the National Company shall be at liberty to pay over to the liquidators of the Tyne Company the dividends which may become payable from time to time to him in the liquidation of the National Company in respect of the 3250L. Then the Tyne Company, who could not be bound to do any such thing, say: "That being so, we will complete the indemnity to Mr. Maitland by undertaking to accept these dividends in lieu of our claims against him." Then as to the statement that Mr. Maitland has already made a transfer to two other persons who are not already accepted by the Tyne Company, whatever may be said about their willingness to accept them, we have the fact before us that at present Mr. Maitland, and no one else, is responsible to the Tyne Company. Once establish the fact that he is a trustee, and, as such, is under liabilities at the request and instance of the cestuis que trust, the cestuis que trust are bound to indemnify him against all the consequences.

As to the question whether a debt will be proved against Mr. Maitland in some other proceeding, there is nothing in this order to pre-

vent the company raising any question they please about that debt. They may apply to prevent the official liquidator from acting on the liberty given him by this order if circumstances arise to justify such a course; but, in the meantime, there is nothing to prevent them from honestly discharging their plain duty, namely, indemnifying their trustee from all the consequences of acting on their behalf. I think it is the simplest case possible, and that the appeal must be dismissed with costs.³

GREENSBORO &c. TURNPIKE CO. v. STRATTON.

1889. 120 Ind. 294, 22 N. E. 247.

OLDS, J.—This is an action to recover for the value of work and labor done and performed by the appellee on the turnpike owned by the appellant at appellant's request, and for gravel and materials furnished by appellee to appellant, and used in the construction and repair of the road-bed and bridges of said turnpike.

The case, as stated by counsel as shown by the evidence, is to the effect that in 1877 the defendant company was organized to build a turnpike, and an amount of capital stock subscribed and directors to manage the affairs of the corporation elected, the appellee being elected one of the directors. The directors collected all the capital stock subscribed, and expended the same in the construction of the road; the funds were insufficient to complete the road; after the funds were exhausted, the directors made an effort to have a tax levied to complete the road, but did not succeed. The directors, then consisting of appellee and Wood and Copeland, agreed by and between themselves to finish the road, appellee to do three-fifths of the work and the others one-fifth each, and, pursuant to this agreement, they completed the road and put it in operation and collected toll for its use. Appellee was from time to time re-elected director, and served as such until the first of the year 1886, when he was succeeded as director, and brought this suit.

The only alleged error properly presented by the record and discussed, is the giving of instruction No. 2 by the court, which instruction is as follows:

"2d. If, at the time the work and labor sued for was done, the plaintiff was a director of the defendant company, no contract or

³ See also, *Shively v. Eureka &c. Min. Co.* (1907) 5 Cal. App. 236, 89 Pac. 1073; *Rider v. Union India Rubber Co.* (1859) 5 Bosw. (N. Y.) 85, (aff'd., 28 N. Y. 379); *Young v. Naval &c. Society, Limited* (1905) 1 K. B. 687, 92 L. T. R. 458 ("But directors being both agents of and trustees for the company are entitled to be indemnified by the company against all losses and expenses properly sustained and incurred by them in the due performance of their office").

As to right of directors to contribution, see *Moxham v. Grant* (1899) 69 L. J. Q. B. 97.—Eds.

agreement between him and his co-directors concerning said work or the price to be paid therefor, or the necessity or propriety therefor, could bind the company. But if the stock and means of the company were exhausted in building the road, and it was impossible by reason thereof to complete the road, and the directors agreed among themselves to complete the road, each doing a portion of the work necessary to finish the road according to the respective amounts of their stock, and charge the same to the company, and, in pursuance thereof, the plaintiff did a portion of the work sued for in finishing and completing the road, and it was to the best interest of said company to do said work, and it was necessary and proper to be done, taking into consideration all the circumstances and conditions of the road, the company would be liable in this action for the reasonable value of work done."

In *Waterman's Law of Corporations*, vol. 2, p. 367, the law is stated as follows: "When a director performs duties outside of those devolving upon him as a director, under an appointment by a resolution of the board, he will be entitled to compensation." Again, in vol. 1, p. 461, it is said: "A director, by resolution of the board, may be empowered to transact any business or agency in behalf of the corporation; and unless there is some agreement express or implied from the circumstances attending appointment, to the contrary, the law will infer a contract on the part of the corporation with its agent, whether he be a director or a stranger, that he shall receive for such service a reasonable compensation."

In the case of *Rogers v. Hastings etc. R. W. Co.*, 22 Minn. 25, the plaintiff was a director of the company, and was, by resolution of the board of directors, appointed land commissioner of the company, and brought suit for his services as such commissioner; and the court says: "To entitle the plaintiff to recover for his services as land commissioner, it was not necessary that he should have received a formal appointment from the board, nor that his employment should have been formally authorized or ratified. If the services were performed under employment by an officer of the company, with the knowledge of the directors, and the company receive the benefit of them without objection, the company is liable upon an implied contract to pay the reasonable worth of the same."

In the case of the *Santa Clara Mining Ass'n. v. Meredith*, 49 Md. 389, the court states the rule of law to be, that "If a president or director of a corporation renders services to his corporation which are not within the scope of, and are not required of him by, his duties as president, or director, but are such as are properly to be performed by an agent, broker or attorney, he may recover compensation for such services upon an implied promise."

This, we think, the true rule, as supported by the great weight of authority. *Chandler v. Monmouth Bank*, 1 Green (N. J.) 255; *Shackleford v. New Orleans, etc.*, R. R. Co., 37 Miss. 202; *New Orleans etc. Co. v. Brown*, 36 La. Ann. 138; *Cheaney v. Lafayette*

etc. R. Co., 68 Ill. 570; Henry v. Rutland etc. R. Co., 27 Vt. 435; Polk v. Reynolds, 54 Ind. 449.

In the case of Ward v. Polk, 70 Ind. 309, it was held that one who was a director of a drainage association could recover on a contract made with the directors of the association for the labor performed by him, notwithstanding he was himself a director. Bristol, etc., Co. v. Probasco, 64 Ind. 406.

We regard the rule of law to be, that when a director of a corporation performs services for the corporation, which are independent and outside of his duties as such director, he has the same right to recover upon an implied contract for such services as though he was not a director, and the same rule applies in regard to materials furnished by a director used by the corporation.

In this case it is conceded that the services rendered and materials furnished were necessary and proper, and enabled the company to finish and put the road in a condition for use, and to receive compensation for travel upon it, which it could not have done without the labor and materials furnished by the appellee, and he is entitled to recover a reasonable compensation for such labor and materials.

We think there is no error in the instruction given by the court of which the appellant can complain.

Judgment affirmed, with costs.

Section 3.—Duties.

A—OBEDIENCE. ACTIONS ULTRA VIRES.

HODGES v. NEW ENGLAND SCREW CO.

1850. 1 R. I. 312.¹

THIS was a bill in equity brought by complainant, a member of the New England Screw Co. against the Company and its directors, charging gross fraud, breach of trust and a violation of the charter.

GREENE, C. J.—There are some questions raised in the present suit, which we find no difficulty in deciding.

We think the directors of the Screw Company are liable in equity, as trustees, for a fraudulent breach of trust. The jurisdiction of a Court of Equity over such a case was affirmed by Lord Hardwicke in the case of The Charitable Corporation v. Sutton and others, (2 Atkins, 404,) in 1742, and has been exercised both in England and in this country ever since. In the case of the Attorney General v. Utica Insurance Company, (2 Johns. Ch. Rep. 359,) Chancellor Kent recognizes the jurisdiction as well settled. In Robinson and others v. Smith and others, (3 Paige 222,) and in Cunningham v.

¹ Statement abridged. Portions of opinion omitted.—Eds.

Pell and others, (5 Paige 607,) the same doctrine is affirmed and acted on. So also by Vice Chancellor McCoun, in *Verplanck v. Mercantile Insurance Company*, (1 Edwards 84). The cases on this point are so numerous, that we deem any farther reference unnecessary.

The primary party, to sue for such fraudulent breach of trust, is the corporation; because the corporation is the party injured. *Robinson and others v. Smith and others*, (3 Paige 222). But if the corporation refuse to sue the stockholders may sue in their individual names. So if the corporation be under the control of the guilty directors, the stockholders may sue. (3 Paige 222. *Ang. & Ames on Corp.*, 304, 305.) * * *

In 1845, the Screw Company were desirous of enlarging their business, and obtained an amendment of their charter, under which they erected a rolling mill, and carried on the business of rolling iron; and, afterwards, finding this unprofitable, went into the business of making railroad iron, and carried on that business until it ceased to be profitable, which was in the latter part of the year 1847. The business was then suspended.

The rolling mill establishment was then without employment. It had cost \$155,000, and was discredited in the market by the unprofitable business which had been carried on there. In erecting the rolling mill establishment, and in carrying on the business there, the Screw Company had incurred a heavy debt. Under these circumstances, the directors of the Screw Company formed the plan of purchasing the nail machine and patent for making wrought nails, and of forming a new company, who were to become the purchasers of the rolling mill and works, and patent and nail machine, and to carry on the business of making wrought nails. The Screw Company were to sell their nail machine and patent, and rolling mill, to the new company at cost, being \$182,000, and to receive \$82,000 in money, and the balance, being \$100,000, in the stock of the new company. The whole capital of the new company was to be \$300,000, to be divided into six hundred shares of five hundred dollars each, of which the Screw Company were to take two hundred shares, provided two hundred shares were taken by others, and the company organized in three months.

One great object of the directors, in making this arrangement, was to effect a sale of their rolling mill upon advantageous terms, and to realize from the sale, in order partially, at least, to relieve themselves from debt.

Another object was the anticipated profits of the new business.

The immediate effect of the arrangement was, that the Screw Company received \$82,000 in cash, for their rolling mill and nail machine and patent, and still retained, as a stockholder in the Iron Company, one-third of the same property, the other subscribers to the Iron Company putting their money against the rolling mill of the Screw Company, at cost.

The plaintiff, although he objected to the purchase of the nail patent and machine, in the first instance, yet afterwards acquiesced in and approved of the measure. And the evidence shows, the directors had strong reasons to believe the purchase an advantageous one. Neither did the plaintiff object to the new company and to the taking stock therein by the Screw Company, but he wished the stock, when taken by the Screw Company, to be divided among the stockholders, and he was not willing that the stock should be taken, except upon these terms.

This conduct of the plaintiff shows, he considered the plan of the directors a judicious one, and for the interest of the Screw Company, for whether the stock were held by the Screw Company, as such, or by the stockholders of that company individually, the business and profits of the Iron Company would be the same.

The answer states, the result of the formation of the Iron Company and the sale of the rolling mill, has been to diminish the liabilities of the Screw Company to the amount of \$15,000, below what they would otherwise have been.

Viewing the plan of the directors, therefore, as a mere business arrangement, and aside from the question of power under the charter, we think it was judicious, and for the interest of the Screw Company. Certainly, we cannot say, they acted without ordinary care and discretion, and, least of all, that they had in view the fraudulent design of reducing the value of the plaintiff's stock in the Screw Company, in order to purchase it at their own price. And we are the more confirmed in this conclusion, when we recollect that the directors owned a large majority of the capital stock of the Screw Company, and could not reduce the plaintiff's stock, without at the same time, and in the same proportion, reducing the value of their own.

The reason given by the directors for not dividing the stock in the Iron Company among the stockholders of the Screw Company, in conformity to the wishes of the plaintiff is, that the Screw Company had incurred a heavy debt by the erection of a rolling mill and the business carried on there, and they thought the consideration received for the sale ought to be held for the payment of that debt.

We do not see anything unreasonable or improvident in this—certainly nothing to sustain the charge of fraud, imputed in the plaintiff's bill. It does not appear that the directors sought or secured to themselves any benefit or advantage, which was not common to all the other stockholders in the Screw Company.¹ * * *

Another question remains to be considered, and that is, are the directors personally liable for taking stock in the Iron Company, not upon the ground of any fraud in fact, on their part, but upon the ground that they violated the charter of the Screw Com-

¹ Various charges of fraud set forth in the bill, were here considered by the court, and found to be unsustained by proof; but as they involved the discussion of no questions of law, they have been omitted in the report.—Eds.

pany, in so doing? In the view we take of the facts upon this part of the case, it is not necessary for us definitely to decide, whether the act under the circumstances, was a violation of the charter of the Screw Company; for, although the charter may have been violated, still, we do not think the directors ought to be personally responsible under the circumstances. We prefer to decide so important a question, upon a proceeding against the corporation, when that is the question directly put in issue. In considering the question of the personal responsibility of the directors, therefore, we shall assume that they violated the charter of the Screw Company. The question then will be, was such violation the result of mistake, as to their powers, and if so, did they fall into this mistake from want of proper care, such care as a man of ordinary prudence practices in his own affairs. [For, if the mistake be such as with proper care might have been avoided, they ought to be liable.] If, on the other hand, the mistake be such as the directors might well make, notwithstanding the exercise of proper care, and if they acted in good faith and for the benefit of the Screw Company, they ought not to be liable.

It was contended by the counsel for the plaintiff, that the ground of innocent mistake could not avail the defendants, because they had not set it up in their answer. But the answer does allege that the directors, in all they have done in managing the affairs of the Screw Company, have acted in good faith and to the best of their ability, skill, and discretion, for the profit and benefit of that Company. This necessarily excludes the idea of a wilful violation of charter, for it is impossible that these defendants could have truly and honestly sworn, they had acted in good faith towards the Screw Company in a matter in which they had knowingly and wilfully violated their charter. It is worthy of observation, too, in this connexion, that the bill nowhere charges that the directors knew the act complained of was a violation of their charter. It charges that the act was done with the design to defraud the plaintiff, and that it was a violation of the charter of the Screw Company; and to this charge the answer is responsive.

Let us look at the circumstances, under which the directors subscribed for this stock.

At the time of the transaction, no case, in which this question of authority was decided or considered, had occurred, either in England or this country. The law on the subject cannot be considered as known and settled.

There are large classes of corporations in Rhode Island and the other States, which may and do rightfully invest their capital in the stock of other corporations; such, for instance, as religious and charitable corporations, and corporations for literary and scientific purposes. So insurance companies may rightfully invest their capital in the stock of other corporations, such as banks and railroads, and the like. Nor have we any doubt that the Screw Company might have rightfully taken this stock in the Iron Company, in payment

for their rolling-mill, if it had been taken with a view to sell again and not permanently to hold it.

Again, it is to be observed, the directors were not investing the dividends of the Screw Company in the stock of the Iron Company. They had on hand an unsaleable rolling-mill, and they owed a heavy debt for it, and one great object in taking the stock in the Iron Company, was to realize for the rolling-mill and in part pay thereby the debt.

The business, too, of the Iron Company was of a kindred nature with that carried on by the Screw Company; and, so far as the manufacture of rods was concerned, intimately connected with the business of the Screw Company.

It was like the case of a corporation for printing calicoes taking stock in the corporation which manufactured and supplied the print cloths. It deserves, also to be remarked in this connection, that this question of power never seems to have been raised by the directors or the stockholders in either company, or, by the plaintiff himself, until the present bill was filed. Under these circumstances, and giving proper weight to the answers of the defendants, we feel bound to say, that in subscribing for this stock, they have acted in good faith and with as much care and discretion, as a man of ordinary prudence exercises about his own affairs, and that, if they have fallen into a mistake in regard to their powers, it was an innocent mistake, for which they ought not to be held answerable. We have in Rhode Island a large number of corporations, whose affairs are managed by directors, who are generally large stockholders and act without compensation. If the innocent mistake of these gentlemen, in cases where the law was unsettled or unknown, is to subject them for damages, great injustice would be done. The law requires of them care and discretion, such as a man of ordinary prudence exercises in his own affairs; and if they practise this, and nevertheless make a mistake, the law does not hold them answerable.

The plaintiff's counsel have referred to the amendment of the Screw Company's charter of October, 1845, as showing that the directors must have known they had no power to take stock in the Iron Company. There were two objects, obtained by that amendment, which could not be obtained without it; one was the right to increase the capital stock to \$300,000, and the other was the right to carry on the business of manufacturing and rolling iron, under the name of the New-England Iron Company. The original charter was for manufacturing purposes, which we think clearly includes the powers to manufacture and roll iron, but it must be done as the original charter stood, under the name of the Screw Company. The amendment in effect, authorized them to adopt a new name; but it did not confer any additional authority to manufacture and roll iron.

Neither do we feel ourselves justified in drawing any inference unfavorable to the defendants, from the fact, that the Screw Com-

pany do not appear among the petitioners for the charter of the Iron Company. * * *

PEOPLE EX REL. PERKINS v. MOSS,

1907. 187 N. Y. 410, 80 N. E. 383.^a

APPEAL from an order of the Appellate Division of the Supreme Court in the first judicial department, entered May 25, 1906, which reversed an order of Special Term dismissing a writ of habeas corpus and directed the discharge of the relator from custody. * * *

The information, upon which the warrant of arrest was issued, charging the relator with the crime of grand larceny in the first degree, was contained in certain depositions taken before the magistrate. One deposition was by Darwin P. Kingsley, a vice-president of the New York Life Insurance Company, which stated that, in December, 1904, when he was secretary of the finance committee of that company, a meeting was had of all of the members of the committee, including McCall, since deceased, who, as president of the company, was ex officio a member. It was stated by the president that, on behalf of the insurance company, he had promised to pay to Cornelius Bliss, as treasurer of the Republican national committee, for use in the presidential campaign of that year, such sums as should not exceed \$50,000, and that Perkins, this relator, then a vice-president of the company, at his, the president's, request and to carry out the agreement with Bliss, had advanced to the latter large sums of money. McCall did not ask the committee to take any official action upon this statement, but desired to inform it of the facts. Conversation was had in regard to the matter and no official action was taken by the committee; but "it was the expressed opinion of those present that McCall should cause Perkins to be reimbursed, for the sums so advanced, out of the funds of the company." It was stated, also, in the deposition that McCall, "by virtue of his office, had power to make disbursements, known as disbursements upon executive order."

Another deposition was by Edmund D. Randolph, a trustee and the treasurer of the insurance company, who was present at the meeting of the finance committee referred to in the deposition of Kingsley, which corroborated Kingsley's statements as to what had taken

^a See also, *Scott v. Depeyster* (1832) 1 Edw. Ch. (N. Y.) 513, esp. 533-5; *Yates v. Jones Nat. Bank* (1906) 206 U. S. 158, 51 L. ed. 1002, 27 Sup. Ct. 638; *London Financial Assn. v. Kelk* (1884), L. R. 26 Ch. Div. 107, 144 (exonerated for "their mere innocent mistake").

Cf. Williams v. McDonald (1886) 42 N. J. Eq. 392, 7 Atl. 866 (liable for loaning money on land not worth double the mortgage); *Leeds & Co. v. Shepherd* (1887) L. R. 36 Ch. Div. 787 (liable for paying dividends out of capital).—Eds.

^b Portion of opinions and dissenting opinion of Werner, J., omitted.—Eds.

place. Randolph stated that some time after the meeting in December, 1904, he drew a check to reimburse Perkins, the relator, for the moneys he had advanced to Bliss; that the payment was made by the treasurer's check to the order of J. P. Morgan & Co., a firm of which Perkins was a member; that this check was drawn by him pursuant to the direction of McCall the president; that, "at that time, large powers were vested in McCall as president to order disbursements to be made from the funds of the company without first submitting for approval to any committee;" that that power had been exercised "upon his sole personal authority" for many years without having been challenged and that Perkins had had nothing to do with the transaction of the drawing of the check, or of the book entries.

GRAY, J.—If the information, which was laid before the magistrate furnished no legal evidence of the commission of a crime by the relator, then he was illegally restrained of his liberty. * * * *

When summed up, the evidence amounts to this: that the president of the company, in whom was vested, and who had for years been exercising, the power to make disbursements of the corporate funds upon his sole authority, had agreed that the insurance company would contribute to the presidential campaign fund of the Republican national committee up to the amount of \$50,000 and that, to protect the company against other demands for political purposes, he requested the relator, one of the company's trustees, to personally carry out the agreement, by advancing the moneys. The relator acquiesced in the president's request, advanced the money and, subsequently, the president brought up the subject of his reimbursement, informally, before a full attendance of the members of the finance committee of the company. The president's purpose was not that the finance committee should take official action in the matter; but that the trustees should be informed of what he had done and that he might have their opinions upon the matter. It was the general opinion that the president should cause the relator to be reimbursed for his advances out of the corporate funds. The facts stated by the witnesses showed that what was brought before this body of the company's trustees was the claim, or right, of Mr. Perkins to be repaid the moneys which he had paid out by the procurement of the president, in order that the latter's agreement on behalf of the company might be carried out, and that the president, exercising the executive power, with which he appears to have been clothed, directed the treasurer of the company to draw the check for the amount of the relator's claim. Furthermore, the prosecution in making use before the magistrate of the relator's letter to the district attorney, as an admission of the facts of the transaction complained of, not only made the fact clear that the moneys were paid out to satisfy the relator's claim, but, also, caused it to appear, affirmatively, that the relator had acted in the honest belief that he was benefiting the company and had derived no personal advantage. The magistrate was not bound to accept the letter as establishing the innocence of the

accused; but, as a part of the evidence used to make out the charge, he had his statements explaining the transaction and stating his honest motives. It was equivalent to his examination.

[It is, unquestionably, true that the purpose, for which the moneys of the company were promised, was foreign to the chartered purposes of the corporation; but that fact does not make the payment a criminal act.] The act not being *malum prohibitum*, nor *malum in se*, the innocent motive of indirectly promoting the corporate affairs, through the supposed advantage of the continuance in power of the Republican administration, purged the act of immorality and it lacked the criminal intent. The company had not the right, under the law of its existence to agree to make contributions for political campaigns, any more than to agree to do other things foreign to its charter; but it had capacity to make agreements, if not prohibited, or inherently wicked. Its act would affect the interests of those concerned with the conduct of the corporate business and effect a private wrong; but it would not be a public offense, or illegal, in the sense of violating any public interest. (*Bissell v. M. S. & N. I. R. R. Co.*, 22 N. Y. 258; *Holmes v. Willard*, 125 ib. 75; *Moss v. Cohen*, 158 ib. 240.) If making the agreement to contribute from the corporate funds was an illegal act, it was because of the limitations upon the corporate powers and not because of considerations of the disadvantage to the company of the act. There are a great many things, which those intrusted with the management of corporate properties are known to do and which they ought not to do, whatever their good motives, not because some statute forbids, but because they are not within the scope of the chartered powers. Their own sense of rectitude and of what is due to those who trust them should admonish them of the wrongful nature of their conduct. It has been well observed that the ultimate welfare of the citizen demands that he shall conform his conduct to the moral law and it concerns him that every one else should conform to it. A moral obligation should be none the less authoritative in the conduct of life that it is binding, only, upon the conscience of the person as a duty and is imperfect in law from the absence of legal sanction. Courts, however, may not sit to judge the conduct of a defendant by any moral code, or rules of ethics. Their sphere is to ascertain if the facts shown establish the crime charged against him. In the facts stated in these depositions I find none, upon which criminality can be predicated. The essential element of the "intent to deprive and defraud" is nowhere to be found and there is no just basis for the inference. There was no concealment about the transaction and knowledge of it was conveyed to the other trustees. That the relator may have made a mistake of law, which will not relieve him from liability in a civil action, may be true, and he expressly disclaimed in his letter any intention to dispute such a liability; but this was a case where the intent, or good faith, was in issue and then knowledge of the law is immaterial. (*Knowles v. City of N. Y.*, 176 N. Y. at p. 439; *Godspeed v. Ithaca St. Ry. Co.*, 184 ib. at p. 354.) The relator came to the aid of the

president of the company, who, as such, had agreed to contribute moneys to the campaign fund, and advanced the moneys, temporarily. Having done so, for no other reason than for the supposed advantage of the company, his claim to be reimbursed from the treasury of the company is openly presented and it is paid. But within the spirit, if not the letter, of section 548 of the Penal Code, that was not larceny. The section provides that "upon an indictment for larceny it is a sufficient defense that the property was appropriated openly and avowedly, under a claim of title preferred in good faith, even though such claim is untenable." This section is an expression of the emphasis which the statute lays upon the intent with which the property of another is taken. It is a qualification of the provisions of section 528 of the Penal Code, defining what shall constitute the crime of larceny. It is of considerable significance, as illustrating the legislative understanding, that when, in 1906, the legislature dealt with the question, specifically, the offense was declared to be a misdemeanor, not a larceny.

The question in this case was whether the facts evidenced the commission of a crime and that was a question of law, which went to the jurisdiction of the magistrate. They showed that the design to injure, the motive to despoil the company, the wrongful purpose were, all, lacking in the information, which was laid before the magistrate and upon which the warrant issued. This being so, the act of the magistrate was wholly without jurisdiction and the warrant and all proceedings under it were absolutely void. (*Hewitt v. Newburger*, 141 N. Y. 538, 543.)

For these reasons, I advise the affirmance of the order appealed from.

HISCOCK, J.—I concur with Judge GRAY in the affirmance of the order appealed from. * * *

We are all agreed upon certain fundamental principles pertaining to this case. The contribution by the president of the New York Life Insurance Company from its funds of \$50,000 to a political campaign committee, even in the absence of any statutory prohibition, was absolutely beyond the purposes for which that corporation existed and was wholly unjustifiable and illegal. And while the contribution was suggested and made by the authority and direction of the president of the company rather than by the relator, still the latter was so a party to the execution of the act that he must be regarded as having aided and abetted it, and, therefore, is criminally responsible if a crime was committed.

Further than this, the assumption will be made without critical analysis of its correctness in all respects, that because the relator understood when he advanced his own funds to Mr. Bliss that the same would be repaid to him with moneys of the corporation, he was from the beginning a party to the plan to appropriate such corporate funds to an unauthorized purpose, and that, therefore, when payment was made to him he did not occupy the position of a bona fide though

mistaken claimant, and does not come within those provisions of section 548 of the Criminal Code which provide that it is a defense to an indictment for larceny "that the property was appropriated openly and avowedly under a claim of title preferred in good faith, even though such claim is untenable."

But, confessedly, these facts and considerations alone are insufficient to justify the charge which has been laid against the relator. At the time of his arrest there was no statute making the contribution of corporate funds to political purposes of itself a crime, and therefore, there must be some evidence that the relator in doing what he did was actuated by a felonious, criminal intent. It is agreed upon all sides that the crime of larceny may not be committed unintentionally, unconsciously or by mistake, but that in order to accomplish it the perpetrator must have the intent referred to. It may be difficult at all times exactly and satisfactorily to define this intent, but the requirement for it as applicable to this case means that when the relator took part in the appropriation of the moneys in question, he must have had in some degree that same conscious, unlawful and wicked purpose to disregard and violate the property rights of another, which the ordinary burglar has when he breaks into a house at night with the preconceived design of stealing the property of its inmates. There is, as there ought to be in the absence of statutory enactment, a long distance between the act which is unauthorized and illegal and which subjects the trespasser to civil liability, and the one which is legally wicked and criminal and which subjects the offender to imprisonment. It is on this point of criminal intent that I think the district attorney has failed to furnish any evidence whatever on which the magistrate might act, although the burden affirmatively rested upon him so to do.

At the outset it must be borne in mind that some of the circumstances which surround this charge are merely accidental and superficial, and not at all decisive. The fact that this contribution was made by the officers of one of those corporations whose management recently has been subjected to grave criticism, and even that it was made for a purpose properly subjected to condemnation and now absolutely prohibited, are of no legal significance. However public opinion or ethics might distinguish them, the legal principles which control the consideration of this case are the same which would be applicable if the president of a manufacturing corporation had contributed from its funds toward the erection of a church supposed to be for the benefit of its employees, or the officers of a railroad company had contributed its funds or the use of its property and transportation facilities for the temporary relief of the sufferers from some sudden and great calamity. We probably should be compelled to say in each case that the contribution was beyond the purposes of the corporation and unauthorized and illegal and the officers making the same civilly liable, but it certainly would be a matter of grave import to hold, in the absence of something else, that they might be prosecuted for stealing.

It, therefore, seems to me that we are justified in scrutinizing with care the depositions presented to the magistrate for the purpose of ascertaining whether they do in fact disclose any intent to commit a crime. * * * *

CULLEN, Ch. J. (dissenting).—I dissent from the decision about to be made. * * * *

It thus appears that by the joint action of the relator and the president of the company this large sum of money was taken from the funds of the company and given to Cornelius Bliss for expenditure for political purposes. Mr. Bliss, neither in his personal nor in his representative capacity had any claim on the company for the money, legal, equitable or moral. The company was to be permanently deprived of it, for it never was to be returned, nor was any consideration to inure to the company for the money paid. The purpose for which it was to be employed was wholly foreign to the business of the corporation and one in which the company had no possible interest, except that of every citizen in the good government of the country. That this was an illegal misappropriation of the company's funds, for which every director or officer engaged therein was personally liable to the corporation, seems to me too clear for debate. A majority of the Appellate Division so held, and as I read the opinion of my brother Gray this court is of the same opinion. Hence it is unnecessary to pursue the discussion of this question further. The relator, therefore, falls exactly within the provisions of the Penal Code, so far as the act is involved, not dealing for the moment with the question of the relator's intent and his belief as to his own authority or that of the president. He has without right deprived the company of its property and appropriated the same to the use of another person not the owner nor entitled to the benefit thereof.

But it is said by the judges of the Appellate Division that the misappropriation of the moneys was simply *ultra vires* and not illegal, and reliance is placed upon a quotation from the opinion of Judge COMSTOCK in *Bissell v. Michigan Southern & N. I. R. R. Co.* (22 N. Y. 258) where he said: "A subscription made by authority of the board of directors and under the corporate seal, for the building of a church or college, or an almshouse, would be clearly *ultra vires*, but it would not be illegal." By a singular fatality there has been entirely overlooked the very next sentence to the one quoted: "If every corporator should expressly assent to such an application of the funds, it would still be *ultra vires*, but no wrong would be committed and no public interest violated."

Doubtless the action or contract of a corporation may be *ultra vires* and yet be vicious in no other respect, but also the action of a board of directors of a corporation may be not only *ultra vires*, but criminal. If a bank should purchase and operate a railroad the action would be, in the absence of any statutory provision on the subject, simply *ultra vires*, and the corporation could not defend an action against it by a passenger for personal injuries on the plea that the

operation of the road was beyond its corporate powers. If, however, the directors of a bank should direct the assets of the corporation to be divided among themselves to the exclusion of the stockholders, the action would not only be ultra vires, but on the part of the directors who might receive the money under the resolution simply theft. The appropriation of the funds or property of a corporation towards an enterprise or business upon which the corporation is not under its charter authorized to embark, is merely ultra vires, if the enterprise is prosecuted for the benefit of the corporation. But when the money or property is applied, not for the use or benefit of the corporation, but for that of third persons, the act is either a tort or a crime, regardless of the question whether the purpose to which the money is applied is one which the corporation under its charter might or might not have pursued. In other words, where the money is applied to the use of a corporation, but to an unauthorized use, it is ultra vires; where it is applied to the use of third parties it is a wrong.

There is this further answer to the argument of the Appellate Division. There is no proof that the corporation authorized the payment to Bliss, and as it would have been an illegal act on the part of the directors (from whom it seems to have been concealed), it must be assumed in the absence of proof to the contrary that it was not authorized. "Power to bind the corporation can be presumed to exist only in its executive agents and officers within the scope of its ordinary business and their ordinary duties." (*First National Bank of Lyons v. Ocean National Bank*, 60 N. Y. 278.) It appears by a statement in one of the affidavits already quoted that the president by virtue of his office "had power to make disbursements known as disbursements upon executive order." Plainly the authority so given to the president was solely to make disbursements for the use and benefit of the corporation. If that is to be construed as an authority for the president to appropriate the moneys of the company for whatever purpose he chose, and for the benefit of any person he might desire to befriend, regardless of any interest of the corporation in the appropriation, then it is sufficient to say that all the parties were engaged in a criminal conspiracy to loot the company, and this instead of relieving the relator from responsibility would emphasize his offense. It must be remembered that the relator was not a mere clerk or subordinate, to whom the word of the president was law, and whose means of livelihood might be dependent on the president's favor, but a trustee and vice-president of the company, and a member of one of the greatest banking firms in the country. He owed the company the duty, not only of abstaining from participating in any misappropriation of the funds by the president, but of aggressive action against the president to prevent or expose such misappropriation. Surely, no one will pretend that the authority so given the president would have authorized the relator to advance, with the agreement for repayment from the company's funds, \$50,000 to buy a diamond necklace for a woman, and there is nothing wrong in buy-

ing a necklace for a woman if a man pays for it with his own money. There is a distinction between the two cases, in that it is even more apparent in the necklace purchase than in the payment to Bliss, that the expenditure was for a subject in which the corporation had no interest. But the very distinction proves that the authority of the president was not unlimited or unqualified. It is only fair to the relator, however, to say that his claim is not that the authority of the president was unlimited, but his belief that the payment was for the benefit of the company, and, therefore, within the authority of the president. * * *

O'BRIEN and EDWARD T. BARTLETT, JJ., concur with GRAY and HISCOCK, JJ.; CHASE, J., concurs with CULLEN, Ch. J., and WERNER, J.

*Order affirmed.*⁴

B—DILIGENCE.

THE CHARITABLE CORPORATION v. SUTTON.

1742. 2 Atk. 400.

The bill was brought to be relieved against the defendants as committeemen, or in other offices, and to have a satisfaction for a breach of trust, fraud, and mismanagement.

LORD CHANCELLOR.—The end of the plaintiff's bill is to be relieved against the defendants, who are fifty in number, and were either committeemen, or in other offices, and to have a satisfaction for a breach of trust, fraud, and mismanagement.

The corporation took its rise from a charter of the crown.

The stock by the charter is not to be less than £20,000 at a time, or more than £30,000.

Several powers were granted for carrying on the affairs of the

⁴In *re Liverpool Household Stores Association*, 62 L. T. R. 873, at p. 875, the court said: "The point to be determined is whether * * * directors who have transgressed their powers can be acquitted of liability on the ground that they considered the position in which they were placed and the instrument of their charter, and honestly concluded that they had authority to do what was proposed and done. It was admitted on the part of the respondents that liability would or might follow transgression not thus excused, but it was urged that an excuse of this kind supported by facts is sufficient, or, in other words, that here, as in the other class of cases, crass negligence must be proved or the indictment will fail. There being no room for denial that this excuse has not availed trustees of wills and settlements, it was attempted to rely on the distinction often noticed between such trustees and directors who, it has been broadly stated, are not trustees. It is a pity to confuse argument by a battle of words. What matters it that directors cannot properly be styled trustees in the generally accepted sense of the term, if, as undoubtedly is the case, they are intrusted with powers exercisable on behalf of others, and for the exercise of which they are therefore accountable to those others?" * * *

corporation, and seven persons appointed under the name of committee-men.

The manner of lending upon pledges, &c., the charter institutes several kinds of officers, particularly one, called the Warehouse-keeper.

It restrains the company from banking, unless with notes payable on demand, and confined within the amount of the stock.

These are the material powers.

The intention of it is extremely plain, to assist poor persons with sums of money by way of loan, to prevent their falling into the hands of pawnbrokers, &c.

In 1724, by the King's sign manual, the stock was enlarged to £100,000, in 1728, to £300,000, and in 1730, to £600,000.

I cannot help observing, as I go along, that this deviation from the original fund, was a handle for all the mischiefs which happened afterwards.

One key of the warehouse was to be in the custody of the warehouse-keeper, another in the cashier's possession, and a third in the bookkeeper's, that each might be a check upon the others.

There was another officer, called the surveyor of the warehouse, whose business it was to examine all the pledges taken in by the warehouse-keeper.

If there was any defect of the goods in value, the warehouse-keeper was to make it good out of his own estate.

It has happened that the most important of these rules was broke through by the court of committee.

agents, or that the limit of their agency is not the mandate of their principals. Why, if they transgress this limit and purport to exercise powers not thereby conferred, should they not be held, as other agents, liable for loss occasioned by their improper conduct?"

In *re National Funds Assur. Co.* (1878) L. R. 10 Ch. Div. 118, Jessel, M. R., said, at p. 128: "I think also they have been guilty, within the meaning of the 165th section, of a 'breach of trust in relation to the company,' by dividing part of the capital among their shareholders, and that they are liable for doing it. Ought I to make them account? I think I ought. As to saying they did it *bona fide*, I think it is impossible to come to that conclusion; a man may not intend to commit a fraud, or may not intend to do anything which casuists might call immoral, and he may be told that to misapply money is the right thing to do, but when he has the facts before him—when the plain and patent facts are brought to his knowledge—as I have often said, and I say now again, I will not dive into the recesses of his mind to say whether he believed, when he was doing a dishonest act, that he was doing an honest one. I cannot allow that man to come forward and say, 'I did not know I was doing wrong when I put my hand into my neighbor's pocket and took so much money out and put it into my own.' It is impossible in a court of justice to call a particular act a *bona fide* act simply because a man says that he did not intend to commit a fraud."

See *Greenfield Savings Bank v. Abercrombie* (1912) 211 Mass. 252, 97 N. E. 897 (valuable review of authorities); *Hill v. Murphy* (1912) 98 N. E. (Mass.) 781; *Brinkerhoff Zinc Co. v. Boyd* (1905) 192 Mo. 597, 91 S. W. 523; *Gilbert v. Finch* (1903) 173 N. Y. 455, 66 N. E. 133, 61 L. R. A. 807, 93 Am. St. 623; In *re New Mashonaland Exploration Co.* (1892) 3 Ch. Div. 577; also article by F. M. Burdick in 7 Col. Law Rev. 387.—Eds.

The cashier was ordered to deliver over the key of the warehouse to the accomptant.

In 1726, John Thompson was appointed warehouse-keeper: he was ordered to deliver over to the messenger and common servants the key of the warehouse.

In September, 1726, the surveyor of the warehouse was discharged, and there was never any appointed afterward; so that all the checks upon the warehouse-keeper were taken away.

Afterward Mr. Woolley and Mr. Warren were appointed assistants to the warehouse-keeper.

It does not appear to me that these persons were any check at all upon the warehouse-keeper, for they gave no security to the corporation, but are rather to be considered as his servants than the servants of the corporation.

So that, from this time, the whole power of pledging, &c., devolved upon these three persons; and from hence the scene of iniquity began, the lending more money upon old pledges, without calling in the first sum lent.

But the general and most destructive method was advancing money several times upon old pledges, which were not worth more than the first sum lent, or else giving credit upon imaginary pledges.

The corporation lent out to Thompson himself, upon these fictitious pledges, large sums of money, notwithstanding he had the whole management of these pledges, so that he might be said to be both borrower and lender.

Woolley and Warren were permitted to act as brokers for the borrowers, and three parts in four of the loans were transacted in their names.

The court of committee took notice of this as an abuse; and that they had printed advertisements, giving directions to persons to apply to them, in order to monopolize the whole brokerage, upon which the committee made an order, that all persons might employ their own brokers; and yet, notwithstanding this, the committee afterward made Woolley and Warren assistants to the warehouse-keeper.

The loss which ensued from this mismanagement is prodigious, for the witnesses have proved very clearly that the money lent was £385,000, whereas the value of the goods pledged was not worth more than £35,000, so that the loss to the corporation is not less than £350,000.

The material consideration for me is, from what causes, and from what persons, this loss may be said to arise.

One set of persons are clearly liable, those who lent the money of the corporation upon fictitious pledges: there were a certain confederacy, or rather conspiracy, who passed in the cause under the name of the partnership of three, or the partnership of four, or of five.

Lord Hardwicke then stated the evidence of John Thompson, the warehouse-keeper, who was examined for the plaintiffs.

It is proved by him, that there was a partnership of five, under a pretense of carrying on a project of mines in Scotland; and that none of the committee knew how the account of the pledges stood, except this partnership of five, four, and three.

The defendants have objected to his evidence, because he was concerned principally in the fraud, and ran away out of the kingdom in order to avoid justice; and besides that, by an act of parliament made in the 6th year of Geo. 2, ch. 2, Thompson is entitled to one-fifth of what he shall discover of the company's effects.

It is very true, this is a legal objection, and though he is not a good witness with respect to the five partners, who have not examined him, yet he is certainly a good witness against such of the defendants as have cross-examined him, and who have thought proper to read his deposition.

The grounds upon which the plaintiffs found their relief against the committeemen are these:

1st, That they have been guilty of manifest breaches of trust, or at least of such supine and gross negligence of their duty, and so often repeated, that it will amount to a breach of trust.

These are great and important questions.

It will be proper to state what are the actual breaches of trust.

1st, Passing of notes, &c.

2dly, Signing notes for loans upon pledges, called renewed pledges, though they knew at the same time that the money originally lent was not paid.

3dly, Signing notes of John Thompson, warehouse-keeper.

4thly, Taking off all the checks upon him, &c.

5thly, Making several orders to put it in the powers of Thompson, Warren, and Woolley, to commit those frauds.

As to the three first, they are actual breaches of trust, and the committee-men are clearly guilty who have been concerned in them.

The bye-law prescribes, that when notes were to be issued by the cashier, they should be signed by one of the committee-men, and intended as a check upon the warehouse-keeper and cashier.

Now several notes have been issued, without observing this rule, which is an express contravention of the bye-law.

A registry of pledges was kept, in which an entry is made of the value of the goods pawned: after this was done, a new loan is made upon the same pledge, to the same person, and a reference to the old number in the registry upon every new advance; so that it may be called a pedigree of loans through twenty descents.

Now it is not in the nature of the thing possible to suppose, that the same person wanting to re-borrow could replace the first money lent; and, therefore, at the outset was a plain and obvious fraud.

I shall therefore direct an inquiry into the value of the goods in general which have been pledged.

As to the third breach of trust, the committee-men's behaviour, with regard to Thompson their warehouse-keeper.

It is such a notorious fraud, or at least gross inattention, to suffer him, who was to set a value on all the pledges, to borrow money upon them himself; that, I shall direct those who shall appear to be guilty of it to make good the loss.

As to the fourth and fifth breach of trust, the taking off all checks upon Thompson, and making several orders to put it in the power of Thompson, Woolley, and Warren, to commit those frauds.

They are not so clearly breaches of trust, though at the same time they appear to me to have tended greatly to the loss and prejudice of the corporation.

But whether they are criminal will be the question. Now I think the persons present are only liable who issued out the orders, which invested Thompson, Woolley, and Warren, with such powers.

But then another head of charge has been made, under the *crassa negligentia*, which has been divided into these several branches:

- 1st, The committee-men's non-attendance upon their employment.
- 2dly, Their not observing the bye-law of law of laying the balance of cash regularly before them.
- 3dly, Not taking any notice of forfeited pledges.
- 4thly, Never once inspecting the warehouse to see what number of real pledges were there.
- 5thly, Putting the whole power into the hands of Thompson, Woolley, and Warren.

Now from all these an accumulated charge is made against the whole body of directors or committee-men.

Consider first the foundation of this general charge.

I take the employment of a director to be of a mixed nature: it partakes of the nature of a public office, as it arises from the charter of the crown.

But it cannot be said to be an employment affecting the public government; and for this reason none of the directors of the great companies, the Bank, South-sea, &c., are required to qualify themselves by taking the sacrament.

Therefore committee-men are most properly agents to those who employ them in this trust, and who empower them to direct and superintend the affairs of the corporation.

In this respect they may be guilty of acts of commission or omission, of mal-feasance or non-feasance. Vide Domat's Civil Law upon this head, 2 B. Tit. 3, secs. 1 and 2.

Now where acts are executed within their authority, as repealing bye-laws and making orders, in such cases, though attended with bad consequences, it will be very difficult to determine that these are breaches of trust.

For it is by no means just in a judge, after bad consequences have arisen from such executions of their power, to say that they foresaw at the time what must necessarily happen; and therefore were guilty of a breach of trust.

Next as to mal-feasance and non-feasance.

To instance in non-attendance; if some persons are guilty of gross non-attendance, and leave the management entirely to others, they may be guilty by this means of the breaches of trust that are committed by others.

By accepting of a trust of this sort, a person is obliged to execute it with fidelity and reasonable diligence; and it is no excuse to say that they had no benefit from it, but that it was merely honorary (ante, 60); and therefore they are within the case of common trustees. Vide *Coggs v. Bernard*, 1 Salk, 26.

Another objection has been made, that the court can make no decree upon these persons which will be just, for it is said every man's non-attendance or omission of his duty is his own default, and that each particular person must bear such a proportion as is suitable to the loss arising from his particular neglect, which makes it a case out of the power of this court.

Now if this doctrine should prevail, it is indeed laying the axe to the root of the tree.

But if, upon inquiry before the Master, there should appear to be a supine negligence in all of them, by which a gross complicated loss happens, I will never determine that they are not all guilty. (So 3 P. W. 215.)

Nor will I ever determine that a court of equity cannot lay hold of every breach of trust, let the person be guilty of it either in a private or public capacity.

The tribunals of this kingdom are wisely formed both of courts of law and equity, and so are the tribunals of most other nations; and for this reason there can be no injury, but there must be a remedy in all or some of them; and therefore I will never determine that frauds of this kind are out of the reach of courts of law or equity, for an intolerable grievance would follow from such a determination.

In the present case one thing is clear, that Sir Archibald Grant, Robinson, Thompson, Burrows and Squire, who were the five that were engaged in that confederacy, are certainly liable to make good the losses which the corporation have sustained in the first place, and the committee-men who were not partners in this affair are liable in the second place only.

Therefore, in the present case, I am of opinion, if there is no evidence to charge the committee-men of being privy to the original design, yet they will be guilty in the second degree, by conniving at the affair, and not making use of the proper power invested in them by the charter, in order to prevent the ill consequences arising from such a confederacy.

I shall begin with such of the defendants as ought to be dismissed, against whom the bill cannot be supported, and then his Lordship names some few of them only.

I shall direct the Master to inquire who were the committee-men that signed notes to Thompson, the keeper of the warehouse, for

they must be responsible for the losses arising from thence, which must be made good by them or their representatives.

I do likewise declare those committee-men to be liable who have issued notes upon loans called renewed pledges, without being signed, and the losses from it to be made good by them or their representatives.

The Master must also state the whole loss the corporation has sustained; and for the better discovery let all books and papers be produced by the several defendants upon oath, and let the plaintiffs by their proper officers produce books and papers on the oath of the said officers.

The late Mr. Aystabie being a committee-man, let his representative appear before the Master to be examined as to the hand his principal had in this affair, and to produce all papers in his custody relating to it.

All other matters must stay until the cause comes back upon the Master's report.⁵

BRIGGS v. SPAULDING.

1890. 141 U. S. 132, 35 L. ed. 662, 11 Sup. Ct. 924.*

This is a bill in equity by the receiver for the First National Bank of Buffalo, brought in the Circuit Court of the United States for the Northern District of New York, against Elbridge D. Spaulding and others, as directors of that bank. The bank was organized under the Acts of Congress in the year 1863.

MR. CHIEF JUSTICE FULLER, after stating the case, delivered the opinion of the court.

In the language of appellant's counsel, the bill was framed upon the theory of a breach by the defendants as directors "of their common law duties as trustees of a financial corporation and of breaches of special restrictions and obligations of the national banking act."

And it is claimed that the defendants should have been held liable

* *Accord*, Overend & Gurney Co. v. Gibb (1872) L. R. 5 H. L. 480; Turquand v. Marshall (1869) L. R. 4 Ch. App. Cas. 376. *Cf.* Leeds & Co. Investment Co. v. Shepherd (1887) L. R. 36 Ch. Div. 787.

In *Dovey v. Cory*, L. R. (1901) App. Cas. 477, at p. 486, Lord Halsbury said: "I cannot think that it can be expected of a director that he should be watching either the inferior officers of the bank or verifying the calculations of the auditors themselves. The business of life could not go on if people could not trust those who are put into a position of trust for the express purpose of attending to details of management. If Mr. Cory was deceived by his own officers—and the theory of his being free from moral fraud assumes under the circumstances that he was—there appears to me to be no case against him at all."

See article, "The Liability of the Inactive Corporate Director," in 8 Columbia Law Rev. 18-26.—Eds.

*Statement abridged. Portions of opinions omitted.—Eds.

for the losses which occurred through loans of the bank's funds and moneys during their term of office as directors, to Lee, his father, his wife and certain designated persons, which were the principal losses, though there were others smaller in amount for which they were responsible.

This liability is alleged to have been incurred by Lee for all loans from October 3, 1881, until April 14, 1882, by F. E. Coit for all losses through the mismanagement of the bank from October 3, 1881, until April 14, 1882, which could have been prevented by reasonable diligence and care on the part of the directors; by John H. Vought on the same basis and for the same time; by Charles T. Coit from October 3 to December 11, 1881; by Cushing from October 3, 1881, to January 10, 1882, unless his liability terminated with the transfer of his stock on the books of the bank; by Spaulding and Johnson from January 10 to April 14, 1882.

It is contended, as an independent proposition, that each of the defendants should have been held liable for all loans made during the periods before mentioned when the loans exceeded ten per cent. of the capital of the bank, in violation of Rev. Stat., § 5200, and also for all loans made while the bank's reserve was below fifteen per cent. of its deposits, in violation of Rev. Stat., § 5191, where such loans resulted in losses.

And finally, that each of the defendants should have been held absolutely liable for all losses of the bank incurred by carrying on its business after its capital became impaired or exhausted and the bank insolvent.

Under Rev. Stat., § 5136, national banking associations were empowered: "Fifth. To elect or appoint directors, and by its board of directors, to appoint a president, vice-president, cashier and other officers, define their duties, require bonds of them and fix the penalty thereof, dismiss such officers or any of them at pleasure, and appoint others to fill their places. Sixth. To prescribe, by its board of directors, by-laws not inconsistent with law, regulating the manner in which its stock shall be transferred, its directors elected or appointed, its officers appointed, its property transferred, its general business conducted and the privileges granted to it by law exercised and enjoyed. Seventh. To exercise by its board of directors, or duly-authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange and other evidences of debt; by receiving deposits; by buying and selling exchange, coin and bullion; by loaning money on personal security; and by obtaining, issuing and circulating notes according to the provisions of this title."

Section 5239 is in these words: "If the directors of any national banking association shall knowingly violate, or knowingly permit any of the officers, agents or servants of the association to violate any of the provisions of this title, all the rights, privileges and fran-

*national
bank (violating
these)*

chises of the association shall be thereby forfeited. Such violation shall, however, be determined and adjudged by a proper circuit, district or territorial court of the United States, in a suit brought for that purpose by the comptroller of the currency, in his own name, before the association shall be declared dissolved. And in cases of such violation, every director who participated in or assented to the same shall be held liable in his personal and individual capacity for all damages which the association, its shareholders or any other person, shall have sustained in consequence of such violation."

When the banking act was originally passed and this bank was organized, that which is now subdivision seven of section 5136 did not contain the words "or duly authorized officers or agents, subject to law"; that is, the original act provided that the board of directors might exercise all such incidental powers as should be necessary to carry on the business of banking, as there specified, but said nothing about the exercise of those powers by the bank officers or agents. The words were inserted in the Revised Statutes, 1873, 1874.

The articles of association of the First National Bank of Buffalo were framed under Rev. Stat., § 5133, and provided for an annual meeting of the stockholders; that the board of directors should appoint a president, cashier and such other officers and clerks as might be required to transact the business of the association and define their respective duties, and by their by-laws specify by what officers of the association or committee of the board the regular banking business of the association should be conducted; and empowered the board of directors to require bonds of the officers. The by-laws of the institution were adopted December 13, 1863, and had relation to the then powers of the board of directors. By section 13 a standing committee was provided for, to be known as the exchange committee, consisting of the president and three directors, appointed by the board every six months, which had power to discount bills, notes, etc., and was required to report at the regular board meetings. Under section 19 a committee was to be appointed every three months to examine into the affairs of the bank and report to the board. Regular meetings were required to be held monthly. It is alleged that on the 7th of January, 1879, the board requested itself to meet thereafter regularly on the first of every month, "to look after the affairs of the bank," etc.

It appears that the provisions of the by-laws were not observed, at least after the amendment in sub-section 7, § 5136, and that the management of the bank was left almost entirely to the officers. No exchange committee nor examination committee was appointed, and the meetings of the board were infrequent and perfunctory. (For years prior to the failure, fourteen at least, the business of the bank had been conducted by the president.)

It is not contended that the defendants knowingly violated, or permitted the violation of, any of the provisions of the banking act, or that they were guilty of any dishonesty in administering the affairs

of the bank, but it is charged that they did not diligently perform duties devolved upon them by the act.

Our attention has not been called, however, to any duty specifically imposed upon the directors as individuals by the terms of the act, although if any director participated in or assented to any violation of the law by the board he would be individually liable. The corporation, after the amendment of 1874, had power to carry on its business through its officers. And although no formal resolution authorized the president to transact the business, yet in view of the practice of fourteen years or more, we think it must be held that he was duly authorized to do so. It does not follow that the executive officers should have been left to control the business of the bank absolutely and without supervision, or that the statute furnishes a justification for the pursuit of that course. Its language does enable individual directors to say that they were guilty of no violation of a duty directly devolved upon them. Whether they were responsible for any neglect of the board as such, or in failing to obtain proper action on its part, is another question. Indeed, it is frankly stated by counsel that "although special provisions of the statute are quoted and relied upon, these do not create the cause of action, but merely furnish the standard of duty and the evidence of wrong-doing"; and section 556 of Morawetz on Corporations is cited, which is to the effect that "the liability of directors for damages caused by acts expressly prohibited by the company's charter or act of incorporation is not created by force of the statutory prohibition. The performance of acts which are illegal or prohibited by law may subject the corporation to a forfeiture of its franchises, and the directors to criminal liability; but this would not render them civilly liable for damages. The liability of directors to the corporation for damages caused by unauthorized acts rests upon the common law rule which renders every agent liable who violates his authority to the damage of his principal. A statutory prohibition is material under these circumstances merely as indicating an express restriction placed upon the powers delegated to the directors when the corporation was formed."

It is perhaps unnecessary to attempt to define with precision the degree of care and prudence which directors must exercise in the performance of their duties. The degree of care required depends upon the subject to which it is to be applied, and each case has to be determined in view of all the circumstances. They are not insurers of the fidelity of the agents whom they have appointed, who are not their agents but the agents of the corporation; and they cannot be held responsible for losses resulting from the wrongful acts or omissions of other directors or agents, unless the loss is a consequence of their own neglect of duty, either for failure to supervise the business with attention or in neglecting to use proper care in the appointment of agents. Morawetz, §§ 551 et seq., and cases.

Bank directors are often styled trustees, but not in any technical

sense. The relation between the corporation and them is rather that of principal and agent, certainly so far as creditors are concerned, between whom and the corporation the relation is that of contract and not of trust. But, undoubtedly, under circumstances, they may be treated as occupying the position of trustees to *cestui que trust*.

In *Percy v. Millaudon*, 8 Martin (N. S.) 68, 74, 75, which has been cited as a leading case for more than sixty years, the Supreme Court of Louisiana, through Judge Porter, declared that the correct mode of ascertaining whether an agent is in fault "is by inquiring whether he neglected the exercise of that diligence and care which was necessary to a successful discharge of the duty imposed on him. That diligence and care must again depend on the nature of the undertaking. There are many things which, in their management, require the utmost diligence, and most scrupulous attention, and where the agent who undertakes their direction, renders himself responsible for the slightest neglect. There are others, where the duties imposed are presumed to call for nothing more than ordinary care and attention, and where the exercise of that degree of care suffices. The directors of banks, from the nature of their undertaking, fall within the class last mentioned, while in the discharge of their ordinary duties. It is not contemplated by any of the charters, which have come under our observation, and it was not by that of the Planter's Bank, that they should devote their whole time and attention to the institution to which they are appointed, and guard it from injury by constant superintendence. Other officers on whom compensation is bestowed for the employment of their time in the affairs of the bank have the immediate management. In relation to these officers the duties of directors are those of control, and the neglect which would render them responsible for not exercising that control properly must depend on circumstances, and in a great measure be tested by the facts of the case. [If nothing has come to their knowledge to awaken suspicion of the fidelity of the president and cashier, ordinary attention to the affairs of the institution is sufficient. If they become acquainted with any fact calculated to put prudent men on their guard, a degree of care commensurate with the evil to be avoided is required, and a want of that care certainly makes them responsible.]"

Spering's Appeal, 71 Penn. St. 11, 20, was the case of a bill filed by Spering, as assignee of a trust company, against its directors and others, to compel them to make good losses sustained by the depositors on the ground of fraudulent mismanagement of the affairs of the company. And Judge Sharswood, speaking for the court, said: "It is by no means a well-settled point what is the precise relation which directors sustain to stockholders. They are, undoubtedly, said in many authorities to be trustees, but that, as I apprehend, is only in a general sense, as we term an agent or any other bailee entrusted with the care and management of the property of another. It is certain that they are not technical trustees. They can

only be regarded as mandatories—persons who have gratuitously undertaken to perform certain duties, and who are therefore bound to apply ordinary skill and diligence, but no more. . . . We are dealing now with their responsibility to stockholders, not to outside parties—creditors and depositors. It is unnecessary to consider what the rule may be as to them. Upon a close examination of all the reported cases, although there are many dicta not easily reconcilable, yet I have found no judgment or decree which has held directors to account, except when they have themselves been personally guilty of some fraud on the corporation, or have known and connived at some fraud in others, or where such fraud might have been prevented had they given ordinary attention to their duties. I do not mean to say by any means that their responsibility is limited to these cases, and that there might not exist such a case of negligence or of acts clearly *ultra vires*, as would make perfectly honest directors personally liable. But it is evident that gentlemen selected by the stockholders from their own body ought not to be judged by the same strict standard as the agent or trustee of a private estate. Were such a rule applied, no gentlemen of character and responsibility would be found willing to accept such places." And see *Citizens' Building Association v. Coriell*, 34 N. J. Eq. 383; *Hodges v. New England Screw Company*, 1 R. I. 312; *Wakeman v. Dalley*, 51 N. Y. 27.

It was in this aspect that Lord Hatherley remarked in *Land Credit Company v. Fermoy*, L. R. 5 Ch. 763, 772: "Whatever may be the case with a trustee, a director cannot be held liable for being defrauded; to do so would make his position intolerable."

And the same view is expressed by Sir George Jessel, M. R., in his opinion in *In re Forest of Dean Coal Mining Co.*, 10 Ch. D. 450, 451, where he says: "One must be very careful in administering the law of joint stock companies not to press so hard on honest directors as to make them liable for these constructive defaults, the only effect of which would be to deter all men of any property, and perhaps all men who have any character to lose, from becoming directors of companies at all. On the one hand, I think the court should do its utmost to bring fraudulent directors to account, and, on the other hand, should also do its best to allow honest men to act reasonably as directors. Wilful default no doubt includes the case of a trustee neglecting to sue, though he might by suing earlier have recovered a trust fund—in that case he is made liable for want of due diligence in his trust. But I think directors are not liable on the same principle."

The theory of this bill is that the defendants are liable, not to stockholders nor to creditors, as such, but to the bank, for losses alleged to have occurred during their period of office, because of their inattention.

If particular stockholders or creditors have a cause of action against the defendants individually, it is not sought to be proceeded

on here, and the disposition of the questions arising thereon would depend upon different considerations.

In *Preston v. Prather*, 137 U. S. 604, 608, it was ruled that gratuitous bailees of another's property are not responsible for its loss unless guilty of gross negligence in its keeping; and whether that negligence existed or not is a question of fact for a jury to determine, or to be determined by the court where a jury is waived. And, further, that the reasonable care which the bailee of another's property entrusted to him for safe-keeping without reward must take, varies with the nature, value and situation of the property, and the bearing of surrounding circumstances on its security. That was a case of persons, engaged in the business of banking, receiving for safe-keeping a parcel containing bonds, which was put in their vaults. They were notified that their assistant cashier, who had free access to the vaults where the bonds were deposited, and who was a person of scant means, was engaged in speculations in stocks. They made no examination of the securities deposited with them, and did not remove the cashier. He stole the bonds so deposited; and it was held that the bankers were guilty of gross negligence, and were liable to the owner of the bonds for their value at the time they were stolen. And Mr. Justice Field, delivering the opinion, said: "Undoubtedly if the bonds were received for safe-keeping, without compensation to them in any form, but exclusively for the benefit of the plaintiffs, the only obligation resting upon them was to exercise over the bonds such reasonable care as men of common prudence would usually bestow for the protection of their own property of a similar character. No one taking upon himself a duty for another without consideration is bound, either in law or morals, to do more than a man of that character would do generally for himself under like conditions."

No one of the defendants is charged with the misappropriation or misapplication of, or interference with, any property of the bank, nor with carelessness in respect to any particular property: but with the omission of duty, which, if performed, would have prevented certain specified losses, in respect of which complainant seeks to charge them.)

Treated as a cause of action in favor of the corporation, a liability of this kind should not lightly be imposed in the absence of any element of positive misfeasance, and solely upon the ground of passive negligence; and it must be made to appear that the losses for which defendants are required to respond were the natural and necessary consequence of omission on their part.

And in this connection the remarks of Mr. Justice Bradley in *Railroad Co. v. Lockwood*, 17 Wall. 357, 382, may well be quoted: "We have already adverted to the tendency of judicial opinion adverse to the distinction between gross and ordinary negligence. Strictly speaking, these expressions are indicative rather of the degree of care and diligence which is due from a party and which he

fails to perform, than of the amount of inattention, carelessness or stupidity which he exhibits. If very little care is due from him, and he fails to bestow that little, it is called gross negligence. If very great care is due, and he fails to come up to the mark required, it is called slight negligence. And if ordinary care is due, such as a prudent man would exercise in his own affairs, failure to bestow that amount of care is called ordinary negligence. In each case the negligence, whatever epithet we give it, is failure to bestow the care and skill which the situation demands; and hence it is more strictly accurate, perhaps, to call it simply 'negligence.' And this seems to be the tendency of modern authorities. If they mean more than this, and seek to abolish the distinction of degrees of care, skill and diligence required in the performance of various duties and the fulfilment of various contracts, we think they go too far; since the requirement of different degrees of care in different situations is too firmly settled and fixed in the law to be ignored or changed."

In any view the degree of care to which these defendants were bound is that which ordinarily prudent and diligent men would exercise under similar circumstances, and in determining that the restrictions of the statute and the usages of business should be taken into account. What may be negligence in one case may not be want of ordinary care in another, and the question of negligence is, therefore, ultimately a question of fact, to be determined under all the circumstances.

The alleged liability of the defendants is such that the facts must be examined as to each of them.

(The learned Chief Justice after examining the facts in detail continued.)

* * * * *

The turning point, so far as defendants Spaulding and Johnson are concerned, (and we include with them Francis E. Coit,) is whether under all the circumstances they were guilty of negligence, producing any of the losses in question, not affirmatively, but because they did not prevent them; and this depends upon whether they should have made an examination of the books and assets of the bank, and whether, if they had, that would have enabled them to discover such a condition of affairs as would have resulted in placing the bank in liquidation, and whether thereby some of the losses would have been averted.

Without reviewing the various decisions on the subject, we hold that directors must exercise ordinary care and prudence in the administration of the affairs of a bank, and that this includes something more than officiating as figure-heads. They are entitled under the law to commit the banking business, as defined, to their duly-authorized officers; but this does not absolve them from the duty of reasonable supervision, nor ought they to be permitted to be shielded from liability because of want of knowledge of wrong-doing, if that ignorance is the result of gross inattention; but in this case we do not

think these defendants fairly liable for not preventing loss by putting the bank into liquidation within ninety days after they became directors, and it is really to that the case becomes reduced at last. For the reasons given, the decree will be

Affirmed.

MR. JUSTICE HARLAN, with whom concurred MR. JUSTICE GRAY, MR. JUSTICE BREWER and MR. JUSTICE BROWN, dissenting.

MR. JUSTICE GRAY, MR. JUSTICE BREWER, MR. JUSTICE BROWN and myself are unable to concur in the opinion and judgment of the court.

We accept, as sufficient, the reasons given for the exemption of the estate of Charles T. Coit and of Cushing from liability for the losses of the bank here in question. But we are of opinion that, under the evidence, the defendants Elbridge G. Spaulding, Francis E. Coit and W. H. Johnson became respectively liable for such of those losses as could have been prevented by proper diligence upon their part as directors. It would serve no useful purpose to refer in detail to all the evidence establishing their dereliction of duty. In our opinion, the proof is clear and convincing that a considerable part of the amount lost to the bank, and therefore to its stockholders and depositors, could have been saved, if they had exercised such care in the supervision and management of the bank's business, as men of ordinary diligence exercise in respect to their own business. In fact, those gentlemen, while they were directors, had no knowledge whatever of what was being done by Lee in the conduct of the bank. They took his word that all was right, and gave no attention whatever to the management of its business. Their eyes were as completely closed to what he did, from day to day, in directing the affairs of the bank, as if they had deliberately determined not to see and not to know how he controlled its business. In the cases of Francis E. Coit and Johnson, there are some mitigating circumstances arising out of the condition of their health, at particular dates, but they are not such as to relieve them from the responsibility they assumed by becoming directors. When Lee asked Johnson to become a director, the latter expressed doubt as to whether he could give the bank much of his time. But Lee said to him that "he could fix that all right." Johnson having, upon one occasion, inquired, in a general way, how the bank was getting on, Lee replied, "nicely;" and Johnson was satisfied. Both Francis E. Coit and Johnson signed reports to the comptroller of the treasury that were false and fraudulent, without having the slightest knowledge of their truth or falsity. They signed and certified to their correctness entirely upon their faith in Lee. They acted as if confidence in him discharged them from all responsibility touching the management of the bank.

In the case of Mr. Spaulding, there are absolutely no circumstances of a mitigating character. He was learned in the law, and had large

experience in banking. He accepted the position of director to accommodate Lee, and without any examination of the condition of the bank. Lee told him the bank was all right, and upon that, and that alone, he rested with implicit confidence. Having taken the oath required by the statute, that he would, so far as the duty devolved upon him, diligently and honestly administer the affairs of the association, and having ascertained that the executive officers were in charge of the bank, performing the duties belonging to their respective positions, he did not, he says, "go any further." Under such circumstances, and as he interpreted the national banking act, he felt himself "relieved from any specified duty." He "had no knowledge of either the provisions of the by-laws or articles of association." In his opinion, if the directors imposed upon the executive officers of the bank the duty of conducting its business, the duties of directors became thereafter "nominal." He performed no duty, while he was director, except "to examine the reports;" but he made no examination to ascertain their correctness. He says: "I regarded my duty as ended, to a great extent, when I saw the bank was in the same charge that it had been." Being asked whether he went to the bank and made an examination of its books, papers or affairs, he replied: "I did not; I took Mr. Lee's word for it." When asked in reference to the enormous overdrafts, made while he was director, and whether he did anything to prevent them, he replied: "I didn't go to the bank to ascertain. I left the officers in charge as I found them." In response to the question whether from the 10th day of January down to the failure of the bank he had anything to do with the affairs of the bank, aside from holding ten shares of its stock, he said: "I never examined its books or affairs, and I only examined the reports which it made to the comptroller, whose duty it was to see that those reports were correct." He never requested any of his co-directors, or any officer of the bank, to call a meeting of the board of directors, for, said he, "that duty was devolved upon the cashier." Lastly, and as sufficient evidence that the directors abandoned to Lee the absolute control of all the bank's affairs and forebore to exercise the slightest control or supervision over him or them, only two meetings of the directors were held from October 3, 1881, until the bank closed its doors on the 14th of April, 1882, *over the whole of which period the dishonest practices of Lee extended*; one, December 12, 1881, for the purpose only of passing resolutions relating to the death of Charles T. Coit, and the other, January 10, 1882, when Spaulding and Johnson were made directors. One of the by-laws provided for regular meetings of the board of directors on the first Tuesday in every month. But he had no knowledge of such a by-law or of any such meetings. It is plain from the evidence that if, with his long experience in banking business, he had given one hour, or at the utmost a few hours' time, in any week while he was director, to ascertain how this bank was being managed, he would have discovered enough that was wrong and reck-

less to have saved the association, its stockholders and depositors, many, if not all, the losses thereafter occurring. Upon his theory of duty, the only need for directors of a national bank is to meet, take the required oath to administer its business diligently and honestly, turn over all its affairs to the control of some one or more of its officers, and never go near the bank again, unless they are notified to come there, or until they are informed that there is something wrong. And when it is ascertained that these officers or some of them, while in full control, have embezzled or recklessly squandered the assets of the bank, the only comfort that swindled stockholders and depositors have is the assurance, not that the directors have themselves diligently administered the affairs of the bank, or diligently supervised the conduct of those to whom its affairs were committed by them, but that they had confidence in the integrity and fidelity of its officers and agents, and relied upon their assurance that all was right. No bank can be safely administered in that way. Such a system cannot be properly characterized otherwise than as a farce. It cannot be tolerated without peril to the business interests of the country.

We are of opinion that when the act of Congress declared that the affairs of a national banking association shall be "managed" by its directors, and that the directors should take an oath to "diligently and honestly administer" them, it was not intended that they should abdicate their functions and leave its management and the administration of its affairs entirely to executive officers. True, the bank may act by "duly authorized officers or agents," in respect to matters of current business and detail that may be properly intrusted to them by the directors. But, certainly, Congress never contemplated that the duty of directors to manage and to administer the affairs of a national bank should be in abeyance altogether during any period that particular officers and agents of the association are authorized or permitted by the directors to have full control of its affairs. If the directors of a national bank choose to invest its officers or agents with such control, what the latter do may bind the bank as between it and those dealing with such officers and agents. But the duty remains, as between the directors and those who are interested in the bank, to exercise proper diligence and supervision in respect to what may be done by its officers and agents.

As to the degree of diligence and the extent of supervision, to be exercised by directors, there can be no room for doubt under the authorities. It is such diligence and supervision as the situation and the nature of the business requires. Their duty is to watch over and guard the interests committed to them. In fidelity to their oaths, and to the obligations they assume, they must do all that reasonably prudent and careful men ought to do for the protection of the interests of others intrusted to their charge.

In respect to the dealings of a bank with others, this court said: "Directors cannot in justice to those who deal with the bank, shut their eyes to what is going on around them. It is their duty to use

ordinary diligence in ascertaining the condition of its business, and to exercise reasonable control and supervision of its officers. They have something more to do than, from time to time, to elect the officers of the bank, and to make declarations of dividends. That which they ought, by proper diligence, to have known as to the general course of business in the bank, they may be presumed to have known, in any contest between the corporation and those who are justified by the circumstances in dealing with its officers upon the basis of that course of business." *Martin v. Webb*, 110 U. S. 7, 15. A rule no less stringent should be applied as between a banking association and directors representing the interests of stockholders and depositors. Subscriptions to the stock of a banking association, and deposits with it, are made in reliance upon the statutory requirement, which cannot be dispensed with, that its affairs are to be managed and administered by a board of directors, acting under oath and with such diligence as the situation requires.

In *Cutting v. Marlor*, 78 N. Y. 454, 460, Chief Justice Church, delivering the unanimous judgment of the court, said: "A corporation is represented by its trustees and managers; their acts are its acts, and their neglect its neglect. The employment of agents of good character does not discharge their whole duty. It is misconduct not to do this, but in addition they are required to exercise such supervision and vigilance as a discreet person would exercise over his own affairs. The bank might not be liable for a single act of fraud or crime on the part of an officer or agent, while it would be for a continuous course of fraudulent practice, especially those so openly committed and easily detected as these are shown to have been. Here were no supervision, no meetings, no examination, no inquiry." This case was referred to, with approval, in *Preston v. Prather*, 137 U. S. 604, 614. So in *Hun v. Cary*, 82 N. Y. 65, 71, which involved the question of the degree of diligence to be exercised by directors of a savings bank, Judge Earl, speaking for the whole court, said: "Few persons would be willing to deposit money in savings banks, or to take stock in corporations, with the understanding that the trustees or directors were bound only to exercise slight care, such as inattentive persons would give to their own business, in the management of the large and important interests committed to their hands. When one deposits money in a savings bank, or takes stock in a corporation, thus divesting himself of the immediate control of his property, he expects, and has the right to expect, that the trustees or directors, who are chosen to take his place in the management and control of his property, will exercise ordinary care and prudence in the trusts committed to them—the same degree of care and prudence that men prompted by self-interest generally exercise in their own affairs. When one voluntarily takes the position of trustee or director of a corporation, good faith, exact justice, and public policy unite in requiring of him such degree of care and prudence, and it is a gross breach of duty—*crassa negligentia*—not to bestow them." Acker-

man v. Halsey, 37 N. J. Eq. 356, 361; Halsey v. Ackerman, 38 N. J. Eq. 501, 510; United Society of Shakers v. Underwood &c., 9 Bush. 609, 621; Horn Silver Co. v. Ryan, 42 Minnesota, 196; United States v. Means, 42 Fed. Rep. 599, 603; Delano v. Case, 121 Illinois 247, 249; Percy v. Millaudon, 3 La. 568, 591; Marshall v. F. & M. Savings Bank of Alexandria &c., 85 Virginia 676, 684; Building Fund Trustees v. Bossieux, 3 Fed. Rep. 817.

These salutary doctrines, if applied to the present case—as, in our judgment, they ought to be—require a reversal, with directions that a decree be entered adjudging Elbridge G. Spaulding, Francis E. Coit's estate and W. H. Johnson liable for such losses occurring during the period in question, as could have been avoided by the exercise of reasonable diligence upon the part of said Coit, Johnson and Spaulding, respectively, in performing the duties appertaining to them as directors. The case is one of supine, continuous negligence, upon the part of the three directors named, in the discharge of duties they owed to the bank and to those interested in it. No usage of a national bank, nor any authority to carry on its business through executive officers and agents, will relieve its directors from the duty imposed upon them by law of diligently managing and diligently administering its affairs, and actively supervising the conduct of its officers and agents. There was here no diligence, no supervision, but absolute inaction in respect to the affairs of the bank.

It was said at the bar that if such a rule be rigidly applied, a gentleman of property and means would hesitate long before accepting the position of director in a banking association. This could not be the result if gentlemen of that class, becoming directors of such institutions, would exercise anything like the care and supervision they or any other prudent, discreet person give to the management of their own business. They ought not, by accepting and holding the position of directors, to give assurance to stockholders and depositors, whose interests have been committed to their control, that the bank is being safely and honestly managed, without doing what prudent men of business recognize as essential to make such an assurance of value. A banking corporation, publicly avowing that its business was to be wholly administered by executive officers, and that the directors would have nothing in fact to do with its management, would not long retain the confidence of stockholders and depositors; a fact which, of itself, shows that the abdication by directors of their duties and functions not only tends to defeat the object for the creation of such an institution, but puts in peril the interests of stockholders and depositors.¹

¹ "It is impossible to give the measure of culpable negligence for all cases, as the degree of care required depends upon the subjects to which it is to be applied. (First Nat. Bank v. Ocean Nat. Bank, 60 N. Y. 278.) What would be slight neglect in the care of a quantity of iron might be gross neglect in the care of a jewel. What would be slight neglect in the care exercised in the affairs of a turnpike corporation, or even of a manufacturing corporation, might be gross neglect in the care exercised in the management of a savings

bank intrusted with the savings of a multitude of poor people, depending for its life upon credit and liable to be wrecked by the breath of suspicion. There is a classification of negligence to be found in the books, not always of practical value and yet sometimes serviceable, into slight negligence, gross negligence, and that degree of negligence intermediate the two, attributed to the absence of ordinary care; and the claim on behalf of these trustees is that they can only be held responsible in this action in consequence of gross negligence, according to this classification. If gross negligence be taken according to its ordinary meaning—as something nearly approaching fraud or bad faith—I cannot yield to this claim; and if there are any authorities upholding the claim, I emphatically dissent from them.

"It seems to me that it would be a monstrous proposition to hold that trustees, intrusted with the management of the property, interests and business of other people, who divest themselves of the management and confide in them, are bound to give only slight care to the duties of their trust, and are liable only in case of gross inattention and negligence; and I have found no authority fully upholding such a proposition. It is true that authorities are found which hold that trustees are liable only for *crassa negligentia*, which literally means gross negligence; but that phrase has been defined to mean the absence of ordinary care and diligence adequate to the particular case." *Per* Earl, J., in *Hun v. Cary* (1880) 82 N. Y. 65, 37 Am. Rep. 546.

"These citations, which might be multiplied, establish, as it seems to me, that while directors are personally responsible to the stockholders for any losses resulting from fraud, embezzlement or wilful misconduct or breach of trust for their own benefit and not for the benefit of the stockholders, for gross inattention and negligence by which such fraud or misconduct has been perpetrated by agents, officers or co-directors, yet they are not liable for mistakes of judgment, even though they may be so gross as to appear to us absurd and ridiculous, provided they are honest and provided they are fairly within the scope of the powers and discretion confided to the managing body." *Per* Sharswood, J., in *Spring's Appeal* (1872) 71 Pa. St. 11, 10 Am. Rep. 684.

"It is to be remembered that they (directors) have the same interests to protect and subserve as other stockholders, and self-interest naturally prompts them to look after their own, and the degree of care they are bound to exercise is that which ordinarily prudent and diligent men would exercise under similar circumstances in respect to a like gratuitous employment, regard being had to the usages of business and the circumstances of each particular case; that they are not liable, in the absence of fraud or intentional breach of trust, for negligence, mistakes of judgment, and bad management in making investments on doubtful or insufficient security. Where they have not profited personally by their bad management, or appropriated any of the property of the corporation to their own use, courts of equity treat them with indulgence." *Per* Pinney, J., in *North Hudson &c. Loan Assn. v. Childs* (1892) 82 Wis. 460, 476 52 N. W. 600, 33 Am. St. 57.

In *Swentzel v. Penn Bank* (1892) 147 Pa. St. 140, 23 Atl. 405, 15 L. R. A. 305, 30 Am. St. 718, held that a bank director cannot be held to the same degree of ordinary care that he takes of his own affairs, "but the ordinary care of a bank director in the business of a bank" (*per* Paxson, J.).

In *Shea v. Mabry* (1878) 1 Lea (Tenn.) 319, followed and approved in *Vance v. Phoenix Ins. Co.* (1880) 4 Lea (Tenn.) 385, held that directors must "exercise reasonable care and diligence, not less, certainly, than they would in their own affairs," the court saying, "No prudent man would have done with his own money as these directors have in this case." (p. 343.)

See also, *Dovey v. L. R.* (1901) App. Cas 477; *Carrington v. Baschor Co.* (1912) 84 Atl. (Md.) 746 ("None of the decisions exact more than a reasonable business knowledge and skill, strict good faith, and a reasonable measure of care and diligence under the circumstances of the particular case"); *Kavanaugh v. Gould* (1911) 147 App. Div. (N. Y.) 281, 131 N. Y. S. 1059, overruling *Kavanaugh v. Commonwealth Trust Co.*

C—LOYALTY.

ABERDEEN RAILWAY COMPANY v. BLAIKIE BROTHERS

1854. 1 Macqueen's App. Cas. 461.⁸

THE action was by Messrs. Blaikie, iron-founders in Aberdeen, against the Railway Company for performance of a contract whereby the Company had agreed to purchase and accept from Messrs. Blaikie certain iron chairs, which they were to manufacture for the Company at the rate of 8l. 10s. per ton. The summons concluded for implement of the contract or for damages.

The principal defence was that Mr. Thomas Blaikie, the managing partner of the Pursuers, was at the time of the contract a Director, and indeed Chairman, of the Railway Company, and so incapacitated from dealing in that character with his own firm.

The Lord Chancellor: * * * This, therefore, brings us to the general question, whether a Director of a Railway Company is or is not precluded from dealing on behalf of the company with himself, or with a firm in which he is partner.)?

The Directors are a body to whom is delegated the duty of managing the general affairs of the Company.

A corporate body can only act by agents, and it is of course the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting. Such agents have duties to discharge of a fiduciary nature towards their principal. And it is a rule of universal application that no one, having such duties to discharge, shall be allowed to enter into engagements, in which he has, or can have, a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect.

So strictly is this principle adhered to that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into.

It obviously is, or may be, impossible to demonstrate how far in any particular case the terms of such a contract have been the best for the interest of the *cestui que trust*, which it was possible to obtain.

It may sometimes happen that the terms on which a trustee has dealt or attempted to deal with the estate or interests of those for

(1909), 64 Misc. (N. Y.) 303, 118 N. Y. S. 758; *Marshall v. Farmers' &c. Bank* (1889) 85 Va. 676, 8 S. E. 586, 2 L. R. A. 534, 17 Am. St. 84; *Gibbons v. Anderson* (1897) 80 Fed. 345 ("The idea is not to be tolerated that they serve as merely gilded ornaments of the institution, to enhance its attractiveness, or that their reputations should be used as a lure to customers"); *Warner v. Penoyer* (1898), 91 Fed. 587, 33 C. C. A. 222, 44 L. R. A. 761; *Rankin v. Cooper* (1907), 149 Fed. 1010.—Eds.

⁸ Statement of facts abridged. Lord Brougham's opinion and portion of Lord Chancellor's opinion omitted.—Eds.

whom he is a trustee, have been as good as could have been obtained from any other person,—they may even at the time have been better.

But still so inflexible is the rule that no inquiry on that subject is permitted. The English authorities on this head are numerous and uniform.

The principle was acted on by Lord King in *Keech v. Sandford* (a), and by Lord Hardwicke in *Whelpdale v. Cookson* (b), and the whole subject was considered by Lord Eldon on a great variety of occasions. It is sufficient to refer to what fell from that very learned and able judge in *Ex parte James*.

It is true that the questions have generally arisen on agreements for purchases or leases of land, and not, as here, on a contract of a mercantile character. But this can make no difference in principle. The inability to contract depends not on the subject matter of the agreement, but on the fiduciary character of the contracting party, and I cannot entertain a doubt of its being applicable to the case of a party who is acting as manager of a mercantile or trading business for the benefit of others, no less than to that of an agent or trustee employed in selling or letting land.

Was then Mr. Blaikie so acting in the case now before us?—if he was, did he while so acting contract on behalf of those for whom he was acting with himself?

Both these questions must obviously be answered in the affirmative. Mr. Blaikie was not only a Director, but (if that was necessary) the Chairman of the Directors. In that character it was his bounden duty to make the best bargains he could for the benefit of the Company.

While he filled that character, namely, on the 6th of February, 1846, he entered into a contract on behalf of the Company with his own firm, for the purchase of a large quantity of iron chairs at a certain stipulated price. His duty to the Company imposed on him the obligation of obtaining these chairs at the lowest possible price.

His personal interest would lead him in an entirely opposite direction, would induce him to fix the price as high as possible. This is the very evil against which the rule in question is directed, and I here see nothing whatever to prevent its application.

I observe that Lord Fullerton seemed to doubt whether the rule would apply where the party whose act or contract is called in question is only one of a body of Directors, not a sole trustee or manager.

But, with all deference, this appears to me to make no difference. It was Mr. Blaikie's duty to give to his co-Directors, and through them to the Company, the full benefit of all the knowledge and skill which he could bring to bear on the subject. He was bound to assist them in getting the articles contracted for at the cheapest possible rate. As far as related to the advice he should give them, he put

^a Select Cases, temp. King, p. 61. ^b 1 Ves. Sen. 8.

his interest in conflict with his duty, and whether he was the sole Director or only one of many, can make no difference in principle.

The same observation applies to the fact that he was not the sole person contracting with the Company; he was one of the firm of Blaikie Brothers, with whom the contract was made, and so interested in driving as hard a bargain with the Company as he could induce them to make.

It can not be contended that the rule to which I have referred is one confined to the English law, and that it does not apply to Scotland.

* * * * *

The principle, it may be added, is found in, if not adopted from, the civil law. In the Digest is the following passage: "*Tutor rem pupilli emere non potest: idemque porrigendum est ad similia; id est ad curatores, procuratores, et qui negotia aliena gerunt.*" Dig., Lib. XVIII., t. 1, c. 34, s. 7.

In truth, the doctrine rests on such obvious principles of good sense that it is difficult to suppose there can be any system of law in which it would not be found. * * *

I have therefore satisfied myself that the Court of Session came to a wrong conclusion.

I therefore move your Lordships that this Interlocutor be reversed.^o

^o In *Metropolitan Elevated R. Co. v. Manhattan Elevated R. Co.* (1884) 11 Daly (N. Y.) 373, 14 Abb. N. C. 103, Van Brunt, J., approving the principal case said: "It will not be denied, I imagine, that as between natural persons, where an agent or trustee has a personal interest opposed to that of the principal, or where a man acts as agent of both parties to the contract, although he may have no personal interest on either side, the principal or cestui que trust may avoid the contract at will, even if there be no actual fraud or damage." * * *

But it is urged that this incapacity does not apply to the directors of a corporation; that the director of a corporation may contract with his corporation, and such contract will be held valid if such contract is shown to be just and fair, because a director of a corporation is not an agent or trustee in the ordinary sense. He is not a trustee of the shareholders, but a trustee of the corporation. * * *

In the case of *Hoyle v. Plattsburgh & Montreal R. R. Co.* (54 N. Y. 314, 328), it was held that the office of director of a railroad company is fiduciary in its character, and, as a consequence, he is incapacitated from dealing in his own behalf in respect to the corporate property or in respect to any matter involving his powers and duties as such director (that this incapacity is not limited to the particular times when he is acting as director, but continues during the period of his directorship. * * * [Actual fraud or actual advantage in such case need not be shown].

The foregoing rule is approved in the case of *Duncomb v. The New York, Housatonic & Northern R. R. Co.* (84 N. Y. 190, 198). * * * The court uses the following language:

"It is not intended to deny or question the rule that whether a director of a corporation is to be called a trustee, or not, in a strict sense, there can be no doubt that his character is fiduciary, being intrusted by others with powers which are to be exercised for the common and general interests of the corporation, and not for his own private interests, and that he falls, therefore,

FORT PAYNE ROLLING MILL v. HILL.

1899. 174 Mass. 224, 54 N. E. 532.

CONTRACT, for money had and received. At the trial in the Superior Court, before Fessenden, J., the jury returned a verdict for the defendant; and the plaintiff alleged exceptions. The facts appear in the opinion.

7. HOLMES, C. J.—This is an action to recover a sum received or retained by the defendant by way of discount upon debts of the plaintiff company which the defendant settled. This discount was or might have been found to have been received by the defendant in pursuance of votes of the directors by which he was employed to settle claims against the plaintiff company, and was to be allowed five per cent. of the face value of bonds used in payment and whatever discount he could get from the claims. He was a director, but took no part in the votes. The main question is whether after the services have been rendered a receiver of the company has the right as matter of law to avoid the contract under which they were ren-

within the doctrine by which equity requires that confidence shall not be abused by the party in whom it is reposed, and which it enforces by imposing a disability, either partial or complete, upon the party intrusted to deal, on his own behalf (citing, *inter alia*, *Aberdeen R. R. Co. v. Blaikie*, 1 Macq. H. L. Cas. 461). Nor is it at all questioned that, in such cases, the right of the beneficiary, or those claiming through him, to avoidance, does not depend upon the question whether the trustee in fact has acted fraudulently or in good faith and honestly, but is founded upon the known weakness of human nature, and the peril of permitting any sort of collusion between the personal interests of the individual and his duties in his fiduciary character. * * *

I think therefore, that the undoubted rule of law in this state is, that every contract entered into by a director with his corporation may be avoided by the corporation within a reasonable time, irrespective of the merits of the contract itself.

But we are asked does this disability extend to the case of a contract between two corporations some of whose directors hold that office in each corporation?

Officer - Director Corp.
I can see no difference in principle between the case of a director contracting with his corporation and that of directors of one corporation contracting with themselves as directors of another corporation. The evils to be avoided are the same; the temptations to a breach of trust are the same; the want of independent action exists and the divided allegiance is just as apparent." (pp. 486, 489, 494-5, 503).

See also, *Sims v. Petaluma Gas Light Co.* (1901) 131 Cal. 656, 63 Pac. 1011; *Pacific &c. Pickle Works v. Smith* (1904) 145 Cal. 352, 78 Pac. 550, 104 Am. St. 42; *Miner v. Belle Isle Ice Co.* (1892) 93 Mich. 97, 53 N. W. 218, 17 L. R. A. 412; *Munson v. Syracuse &c. R. Co.* (1886) 103 N. Y. 58, 8 N. E. 335 (cf. *McNab v. McNab &c. Mfg. Co.* (1891) 62 Hun (N. Y.) 18, 16 N. Y. S. 448, 41 N. Y. St. 906, *affd. short* [1892] 133 N. Y. 687, 31 N. E. 627); *Jacobson v. Brooklyn Lumber Co.* (1906) 184 N. Y. 152, 76 N. E. 1075; *Attala Iron Ore Co. v. Virginia &c. Coke Co.* (1903) 111 Tenn. 527, 77 S. W. 774.

As to consent or ratification of stockholders, see *U. S. Steel Corp. v. Hodge* (1902) 64 N. J. Eq. 807, 54 Atl. 1; *Goss & Co. v. Goss* (1911) 147 App. Div. (N. Y.) 698, 132 N. Y. S. 76.—Eds.

dered. The jury have found that all parties acted in good faith and that the contract was not improvident. They may have found more specifically that the defendant advanced his own money to settle the claims, that the claims were secured by liens and were being pressed, and that the company had no other way of raising money. We are not prepared to say that the receiver may avoid the contract now. If made with any one else, it would have been binding. It was not illegal or void because made with a director, the only person likely to be willing to make it. In this country it very generally has been deemed impracticable to adopt a rule which absolutely prohibits such contracts. *Nye v. Storer*, 168 Mass. 53, 55. Whatever small conflict of interest between himself and the company there may have been, was no greater or other than that between a broker paid by a percentage and his principal. It was manifest and must have been understood. The contract called for action outside the defendant's duty as director, or at least, on the defendant's evidence, needed such action before it could have any effect, for it was no part of the defendant's duty as director to advance his own money. Assuming the contract to have been a provident one, ~~that~~ it well may have been, and as the jury have found that it was, it seems to us not much more open to objection than a contract with a managing director to pay him a salary.

It is argued that the defendant did not pursue the votes because he bought the claims and held them as security for the sums advanced by him. But under the terms of the arrangement with the defendant, the course adopted did not in any way tend to the disadvantage of the company, and we must take it that the jury have found, as they had a right to find, that the purchase was merely a step in a transaction which ended, and from the beginning was intended to end, in the payment of the claims. It does not seem to us that a more definite discussion of the rulings asked and given is necessary.

*Exceptions overruled.*¹⁰

¹⁰ Cf. *Dixon, J.*, in *Stewart v. Lehigh Valley R. Co.* (1875) 38 N. J. L. 505, at p. 523: "Nor is it proper for one of a board of directors to support his contract with his company, upon the ground that he abstained from participating as director in the negotiations for and final adoption of the bargains by his co-directors; the very words in which he asserts his right declare his wrong; he ought to have participated, and in the interest of the stockholders, and if he did not, and they have thereby suffered loss, of which they shall be the judges, he must restore the rights he has obtained—he must hold against them no advantage that he has got through neglect of his duty toward them."

In *Haas v. Universal &c. Record Co.* (1912) 132 N. Y. S. 767, the three directors of defendant corporation "met and unanimously voted themselves a salary of \$50 a month each 'for services actually to be rendered to this company.'" *Held*, the directors could not recover, the court saying: "There is no proof of the value of the services, and they were apparently accepted by the corporation acting only through the same officers. The plaintiff cannot, therefore, recover either under an express or implied contract."—Eds.

SCHNITTGER v. OLD HOME ETC. MIN. CO.

1904. 144 Cal. 603, 78 Pac. 9.

APPEAL from a judgment of the Superior Court of Nevada County and from an order denying a new trial. F. T. Nilon, Judge.

The facts are stated in the opinion.

HARRISON, C.—The Old Home Consolidated Mining Company is a corporation organized under the laws of this state, and having a board of five directors, who at the times herein considered were John McKewen, George T. Emery, Walter McG. Logan, F. Hahn, and C. W. Weld. August 16, 1897, it executed to the plaintiff's assignor its promissory note for five thousand dollars, payable two years thereafter, with interest at the rate of one per cent. a month, and at the same time, for the purpose of securing its payment, executed a mortgage upon certain mining property within this state. The promissory note was also indorsed by each of its directors. The execution of the mortgage was duly authorized by a vote of more than two-thirds of its stockholders at a meeting called for that purpose. Prior to its maturity the note was assigned to the plaintiff. Interest on the note was paid by the corporation up to August 16, 1901. October 8, 1901, the present action was brought against the corporation and C. W. Weld and Walter McG. Logan, two of the indorsers, to recover the amount of the note and for a foreclosure of the mortgage. The action was defended upon the ground that the money for which the promissory note was given and the mortgage executed was the money of, and furnished by, the directors Hahn and McKewen; that they are the real parties in interest in the transaction, and that they entered into it for the purpose of foreclosing the mortgage and obtaining the property of the corporation; that in so doing they violated their duties as trustees, and that for this reason the note and mortgage were void.

Upon the trial of the cause the court found that the corporation defendant had received the five thousand dollars for which its promissory note and mortgage had been executed, and that the transaction was thereafter ratified by the vote of more than two-thirds of its stockholders; that the money loaned to it was in fact the money of the directors Hahn and McKewen, and that they are the real parties in interest in the note and mortgage; that the note was made in the name of Helene Mayer; that the note and mortgage were given to and in her name with the purpose and object on the part of said Hahn and McKewen to obtain control of the property of the corporation; that the assignment from her to the plaintiff herein was not a *bona fide* transaction; that the name of the plaintiff was inserted in said assignment in order to cover up the interest of said Hahn and McKewen, and to give it the appearance of an actual *bona fide* transaction; that at the meeting of the board of directors of the defendant corporation, at which the loan was authorized, all of

the directors were present, and that Hahn and McKewen participated therein; that at that meeting it was stated to the board by the attorney of Helene Mayer that the loan could be obtained from her, and that the directors, other than Hahn and McKewen, believed that the money would be furnished by her; that Hahn and McKewen did not at that meeting or any other time state from whom the loan was to be obtained. The court also found that interest had been paid upon the note up to August 16, 1901, and that since that date no interest had been paid, and held that the plaintiff is entitled to no further interest.

Upon these findings the court held that the plaintiff was entitled to judgment against the defendants for the sum of five thousand dollars, without any interest thereon, together with three hundred dollars as counsel fees, and one hundred dollars for costs of receiver, and for a decree of foreclosure against the defendant corporation, and sale of the mortgaged property to satisfy said amount. From the judgment thus entered the defendants have appealed upon the judgment roll alone, without any bill of exceptions.

The appellants do not question the sufficiency of the evidence to sustain the findings of the court, or claim that the evidence before the court would have authorized any further or different findings, but urge in support of their appeal that as Hahn and McKewen were directors of the corporation defendant their relation to the corporation and to its stockholders was that of trustees, and that by virtue of that relation the transaction in which the loan was made to the corporation was void.

A director of a corporation, like any other trustee, is bound to act in the utmost good faith toward his beneficiary (Civ. Code, sec. 2228), and is forbidden to take part in any transaction concerning the trust in which he has an interest adverse to that of his beneficiary (Civ. Code, sec. 2230); but he is not absolutely precluded from dealing directly with the corporation of which he is a director. Any transaction between them is subject to rigid scrutiny, and is voidable at the instance of the beneficiary for any violation of his duty as trustee, but is not ipso facto void. "The mere fact that the creditor was a director of the company does not render the transaction fraudulent. There is nothing which forbids either members or directors of a corporation from making contracts with it like any other individual; and when the contract is made, the director stands as to the contract in the relation of a stranger to the corporation." (Stratton v. Allen, 16 N. J. Eq. 229.) Mr. Thompson says (3 Thompson on Corporations, sec. 2068): "We therefore find the prevailing doctrine to be, that the director of a corporation may advance money to it, may become its creditor, may take from it a mortgage or other security, and may enforce the same like any other creditor, but always subject to severe scrutiny and under the obligation of acting in the utmost good faith." (See, also, Taylor on Corporations, sec. 634; Twin Lick Oil Co. v. Marbury, 91 U. S. 587; Beach v. Miller, 130

Ill. 162;¹ *Santa Cruz R. R. Co. v. Spreckles*, 65 Cal. 193; *Sutter-Street R. R. Co. v. Baum*, 66 Cal. 44; *Pauly v. Pauly*, 107 Cal. 8;² *Phillips v. Sanger Lumber Co.*, 130 Cal. 431.)

The question presented upon this appeal does not involve the validity of a transaction in which the director of a corporation has executed a contract on behalf of the corporation in which he is personally interested, without any previous authority of the corporation, or where the resolution authorizing its execution depended upon his vote therefor. The transaction was had under the authority of the corporation, given at a meeting of the board of directors at which all were present, and although the court finds that at that meeting Hahn and McKewen "were present and participated therein," it does not find that they voted upon the proposition for the loan. But, even if they had voted for it, the transaction would not have been thereby vitiated, inasmuch as the votes of the other three members of the board were sufficient to make the resolution effective. (*Porter v. Lassen County etc. Co.*, 127 Cal. 261.) It was not a fraud upon the corporation, or upon the other members of the board, for these directors not to disclose the fact that they were the real parties who were loaning the money, or that the person in whose name the transaction was had was merely a figurehead. It was no violation of their duty as trustees to loan the money in the name of another rather than in their own, unless it could be shown that thereby the corporation sustained some detriment, or they obtained some undue advantage over the corporation

The allegation in the answer that Hahn and McKewen procured the loan to be made in the name of Helene Mayer for the sole purpose at that time to bring suit to foreclose said mortgage and finally acquire the title to the mining property of said corporation in violation of their trust, is not found by the court to be a fact, and it must be assumed that there was no evidence tending to establish that allegation. The finding that the money was loaned and the note and mortgage given in her name "with the purpose and object on the part of said Hahn and McKewen, and both of them, of obtaining control of the property of said corporation" does not entitle the corporation to avoid its agreement and retain the money. Whatever may have been the underlying motive for entertaining this purpose, the corporation was in no respect injured thereby. They could obtain control of the mortgaged property only through a sale at public auction under a decree of foreclosure. If they should become the purchasers at such sale, the property would still be subject to redemption either by the corporation, or, in its behalf, by any of its stockholders. (*Wright v. Oroville Mining Co.*, 40 Cal. 20.) The transaction was not concealed from the stockholders; the resolution authorizing it was spread upon the records of the corporation; Hahn and McKewen, as well as the other directors, indorsed the note, and the note

¹ 17 Am. St. 291, and note.

² 48 Am. St. 98.

and mortgage were recorded in the county recorder's office, and thereafter the stockholders ratified the transaction.

The judgment should be affirmed.

COOPER, C., and GRAY, C., concurred.

For the reasons given in the foregoing opinion the judgment and order appealed from are *affirmed*.

SHAW, J., ANGELLOTTI, J., VAN DYKE, J.^{10a}

BOOTH v. ROBINSON.

1880. 55 Md. 419, 439-442.¹¹

ALVEY, J. * * *

In this case, the fact that Robinson and Shoemaker were stockholders and directors in the Steam Packet Company, as well as in

^{10a} Clark v. American Coal Co. (1892) 86 Ia. 436, 53 N. W. 291, 17 L. R. A. 557; Jesup v. Illinois Central R. Co. (1890) 43 Fed. 483 (per Harlan, J.), *Accord*.

"There is some confusion among the cases as to what contracts between a company and a director or officer thereof are void or merely voidable. It is well settled however, that a director cannot make with himself or for his own benefit a contract which will bind the company; and an agreement to pay a director a stipulated sum, which depends upon the vote of such director, is void, and no recovery can be based upon such contract." Gardner v. Butler, 30 N. J. Eq. (E. & A.) 702. Under the laws of California, the legal domicile of the bankrupt, which settles the powers of the board of directors in this respect, such resolution is void and not merely voidable, as McCarthy's personal interest disqualified him not only from voting on the resolution, but also from furnishing the necessary presence at such meeting to constitute a quorum that an affirmative vote on such resolution might be had. Curtin v. Salmon River, etc. Co., 130 Cal. 345, 62 Pac. 552, 80 Am. St. 132." Rellstab, J., in In re McCarthy Portable Elevator Co. (1912) 196 Fed. 247. To similar effect, see Wickersham v. Crittenden (1892) 93 Cal. 17, 28 Pac. 788, (1895) 110 Cal. 332, 42 Pac. 893; Adams v. Burke (1903) 201 Ill. 395, 66 N. E. 235 ("The law is, that where a salary or compensation is voted to an officer, the resolution is illegal if it is carried by his vote or produced by his influence, where he has a controlling interest").

In Higgins v. Lansingh (1895) 154 Ill. 301, 40 N. E. 362, *held* that a director's contract is voidable without regard to good faith or fairness, if there is no disinterested majority. Carter, J. said (pp. 367-8): "* * * so long as a corporation remains solvent, its directors may, with knowledge of its stockholders, deal with it, loan it money, take security or buy property of it, the same as a stranger. * * * But it has not been held that the company or its stockholders may not avoid a contract requiring the action of the board of directors to make it, whether made in good faith or not, where so many of the directors are interested in the contract adversely to the company that the company is not represented by a disinterested majority of the directors voting. On the contrary, it is held that the directors, without the sanction of the stockholders, have no power to contract, for the corporation, with themselves or for the benefit of themselves, and if they attempt to do so the contract may be avoided by the corporation or its stockholders not consenting, whether the contract appears to be fair and just or not." And so, Mobile Land Improvement Co. v. Gass (1904) 142 Ala. 520, 39 So. 229.—Eds.

¹¹ Only a portion of the opinion is given.—Eds.

the Powhatan Company, and participated in the transactions between the two companies, with certain interest in other companies, supposed to be interested, would seem to constitute the main foundation for the principal charges of the bill. And if it be true, as charged by the plaintiffs, that the two defendants, Robinson and Shoemaker, acting for and in behalf of the Steam Packet Company, did purchase the stock in the Powhatan Company, and procure themselves to be elected directors therein, for the purpose of getting control of the management of that corporation, and by that means to make it subservient to the interest of rival companies, or with the design of making insolvent and utterly breaking down the corporation altogether, and thus getting rid of competition, no more flagrant fraud could be perpetrated; and there can be no question but that for all loss to the company or its stockholders, resulting from the carrying out of such device or contrivance, the guilty parties should be held responsible to the fullest extent allowed by the law. Not only would there be incurred a personal responsibility by the directors or agents participating in the wrong, but, if such a scheme were devised and executed at the instance and on behalf of another corporation, deriving its powers and franchises from the State, such conduct would be a fraud upon the State; and in addition to incurring civil liability for the injury done, such conduct would subject the offending corporation to the penalties of misuser or abuser of its franchises. A corporation cannot be allowed to do indirectly and covertly, what it is not authorized to do directly and openly. And whenever such an attempt is made, the Courts can neither be too emphatic in condemning the act, nor too ready to afford the strongest remedy allowed by the law for the prevention or redress of the wrong.

Such is the law as applicable to the case as stated in the bill. But if, upon the proof, there is a failure to establish the fraudulent design or purpose alleged to have characterized the various acts and transactions done and instigated by the two directors named, the whole foundation of the case fails. [For, as we have seen, mere indiscretion, want of skill or foresight, or mistakes of judgment, in the conduct of the affairs of the corporation, afford no ground of personal liability on the part of the directors.]

And upon the question of the fraudulent intent or design charged, though it be true that these two directors represented both corporations,—in the one, being two of a board of eight directors, and in the other, two of a board of six directors,—this fact alone, while it should subject their conduct to rigid scrutiny by the court, does not afford ground of presumption against the legality and fairness of the dealings and transactions between the two companies. The two companies were certainly competent to contract the one with the other; and the two directors whose conduct is in question were interested in both companies, and by their relation to and official positions in them, they owed duties, and were bound to be faithful alike, to both. Therefore, while acting within the scope of the powers delegated to

them by the stockholders of the corporation, there is no presumption of illegality or unfairness in their dealings and transactions as between the two companies. They were the chosen agents of both; and to be successful in any attempt to impeach the validity of their acts, with a view of making them personally responsible either to the corporation or to the stockholders, there must be distinct charges of misconduct, fully supported by proof. *Adams Mining Co. v. Senter*, 26 Mich. 73; *U. S. Rolling Stock Co. v. Atlantic & Great Western R. Co.*, 34 Oh. St. 450.

This case is altogether unlike that of a trustee, agent, or director, bargaining in a matter of personal advantage to himself individually, with the party reposing the confidence in him, and where it is incumbent upon him to show that a fair and reasonable use has been made of that confidence; as in the cases of the *Hoffman Steam Coal Co. v. Cumbld. Coal & Iron Co.*, 16 Md. 456; *Cumbld. Coal & Iron Co. v. Parish*, 42 Md., 598; *Jackson v. Ludeling*, 21 Wall., 616, and other cases of that class to which reference might be made. In that class of cases the law proceeds upon the principle of constructive fraud, irrespective of fraud in fact, and hence the onus of proof is upon the party seeking to maintain the transaction. But in a case like the present, where the effort is to make the defendants personally liable for alleged injuries occasioned by conduct wilfully fraudulent, in intent and purpose, amounting to breaches of trust, the proof in support of the allegations must be other than mere constructive fraud or breaches of trust;—there must be affirmative proof of the misconduct charged, going to establish the fraud in fact.

Such being the requirement of the case, the motive and intent with which the various acts were done, or left undone, by the directors, and charged as fraudulent, become most material. * * *

²² *San Diego & C. R. Co. v. Pacific Beach Co.* (1896) 112 Cal. 53, 44 Pac. 333, 33 L. R. A. 788; *Smith v. Wells Mfg. Co.* (1897) 148 Ind. 333, 345, 46 N. E. 1000; *Aldine Mfg. Co. v. Phillips* (1902) 129 Mich. 240, 88 N. W. 632; *Robotham v. Prudential Ins. Co.* (1903) 64 N. J. Eq. 673, 53 Atl. 842; *McComb v. Barcelona Apartment Assn.* (1892) 134 N. Y. 598, 31 N. E. 613; *Roy & Co. v. Scott, Hartley & Co.* (1895) 11 Wash. 399, 39 Pac. 679, *Accord.* But see *Fitzgerald v. Fitzgerald etc. Const. Co.* (1895) 44 Neb. 463, 62 N. W. 899 (writ of error dismissed 160 U. S. 556, 16 Sup. Ct. 389, 40 L. ed. 536); *Metropolitan Elevated R. Co. v. Manhattan Elevated R. Co.* (1884) 11 Daly (N. Y.) 373, esp. 514-5, 14 Abb. N. C. (N. Y.) 103 (voidable although fair); *Ernest v. Nicholls* (1857) 6 H. L. Cas. 401.

See also *O'Conner & C. Mfg. Co. v. Coosa Furnace Co.* (1891) 95 Ala. 614, 10 So. 290, 36 Am. St. 251; *Continental Ins. Co. v. New York etc. R. Co.* (1907) 187 N. Y. 225, 79 N. E. 1026 (assent of majority of shareholders ratifies transaction made by interlocking directors on two boards); *National & C. Beam Co. v. Chicago & C. Equipment Co.* (1907) 226 Ill. 28, 80 N. E. 556 (invalid because of personal interest of mutual officers).

Cf. Evansville Public Hall Co. v. Bank of Commerce (1894) 144 Ind. 34, 42 N. E. 1097 (transaction valid if fair, although no disinterested majority).

In *San Diego & C. R. Co. v. Pacific Beach Co.*, (1896) 112 Cal. 53, 44 Pac. 333, 33 L. R. A. 788, *McFarland, J.*, said: "Where two corporations, through their boards of directors, make a contract with each other, the directors who are common to both are not within the rigid rule of the cases which

TWIN-LICK OIL CO. v. MARBURY.

1875. 91 U. S. 587, 23 L. ed. 328.¹⁸

MR. JUSTICE MILLER delivered the opinion of the court.

The appellant here, complainant below, was a corporation organized under the laws of West Virginia, engaged in the business of raising and selling petroleum. It became very much embarrassed in the early part of 1867, and borrowed from the defendant the sum of \$2,000, for which a note was given, secured by a deed of trust, conveying all the property, rights, and franchises of the corporation to William Thomas, to secure the payment of said note, with the usual power of sale in default of payment. The property was sold under the deed of trust; was bought in by defendant's agent for his benefit, and conveyed to him in the summer of the same year. The defendant was, at the time of these transactions, a stockholder and director in the company; and the bill in this case was filed in April, 1871, four years after, to have a decree that defendant holds as trustee for complainant, and for an accounting as to the time he had control of the property. It charges that defendant has abused his trust relation to the company, to take advantage of its difficulties, and buy in at a sacrifice its valuable property and franchises; that, concealing his knowledge that the lease of the ground on which the company operated included a well, working profitably, and by promises to individual shareholders that he would purchase in the property for the joint benefit of the whole, he obtained an unjust advantage, and in other ways violated his duty as an officer charged with a fiduciary relation to the company. As to all this, which is denied in the answer, and as to which much testimony is taken, it is sufficient to say that we are satisfied that the defendant loaned the money to the corporation in good faith, and honestly to assist it in its business in an hour of extreme embarrassment, and took just such security as any other man would have taken; that when his money became due, and there was no apparent probability of the company paying it at any time, the property was sold by the trustee, and bought in by defendant at a fair and open sale, and at a reasonable price; that, in short, there was

hold that one who acts in a fiduciary capacity cannot deal with himself in his individual capacity, and that any contract thus made will be declared void without any examination into its fairness, or the benefits derived from it to the cestui que trust. } Two corporations have the right, within the scope of their chartered powers, to deal with each other; and this right is certainly not destroyed or paralyzed by the fact that some, or a majority, of the directors are common to both. Of course, if such directors should wrongfully and wilfully use their powers to the prejudice of one of the corporations, their action, if not acquiesced in, and if contested at the proper time, could be avoided, as in any other case of actual fraud. But such common directors owe the same fidelity to both corporations, and there is no presumption that they will deal unfairly with either; therefore their acts as such common directors are not void," referring to numerous authorities.—Eds.

¹⁸ Portion of opinion omitted.—Eds.

neither actual fraud nor oppression, no advantage was taken of defendant's position as director, or of any matter known to him at the time of the sale, affecting the value of the property, which was not as well known to others interested as it was to himself; and that the sale and purchase was the only mode left to defendant to make his money.

The first question which arises in this state of the facts is, whether defendant's purchase was absolutely void.

That a director of a joint-stock corporation occupies one of those fiduciary relations where his dealings with the subject-matter of his trust or agency, and with the beneficiary or party whose interest is confided to his care, is viewed with jealousy by the courts, and may be set aside on slight grounds, is a doctrine founded on the soundest morality, and which has received the clearest recognition in this court and in others. *Koehler v. Black River Falls Iron Co.*, 2 Black, 715; *Drury v. Cross*, 7 Wall. 299; *Luxemburg R. R. Co. v. Maquay*, 25 Beav. 586; *The Cumberland Co. v. Sherman*, 30 Barb. 553; 16 Md. 456. The general doctrine, however, in regard to contracts of this class, is, not that they are absolutely void, but that they are voidable at the election of the party whose interest has been so represented by the party claiming under it. We say, this is the general rule: for there may be cases where such contracts would be void ab initio; as when an agent to sell buys of himself, and by his power of attorney conveys to himself that which he was authorized to sell. But, even here, acts which amount to a ratification by the principal may validate the sale.

The present case is not one of that class. While it is true that the defendant, as a director of the corporation, was bound by all those rules of conscientious fairness which courts of equity have imposed as the guides for dealing in such cases, it cannot be maintained that any rule forbids one director among several from loaning money to the corporation when the money is needed, and the transaction is open, and otherwise free from blame. No adjudged case has gone so far as this. Such a doctrine, while it would afford little protection to the corporation against actual fraud or oppression, would deprive it of the aid of those most interested in giving aid judiciously, and best qualified to judge of the necessity of that aid, and of the extent to which it may safely be given.

There are in such a transaction three distinct parties whose interest is affected by it; namely, the lender, the corporation, and the stockholders of the corporation.

The directors are the officers or agents of the corporation, and represent the interests of that abstract legal entity, and of those who own the shares of its stock. One of the objects of creating a corporation by law is to enable it to make contracts; and these contracts may be made with its stockholders, as well as with others. In some classes of corporations, as in mutual insurance companies, the main object of the act of incorporation is to enable the company to make

contracts with its stockholders, or with persons who become stockholders by the very act of making the contract of insurance. It is very true, that as a stockholder, in making a contract of any kind with the corporation of which he is a member, is in some sense dealing with a creature of which he is a part, and holds a common interest with the other stockholders, who, with him, constitute the whole of that artificial entity, he is properly held to a larger measure of candor and good faith than if he were not a stockholder. So, when the lender is a director, charged, with others, with the control and management of the affairs of the corporation, representing in this regard the aggregated interest of all the stockholders, his obligation, if he becomes a party to a contract with the company, to candor and fair dealing, is increased in the precise degree that his representative character has given him power and control derived from the confidence reposed in him by the stockholders who appointed him their agent. If he should be a sole director, or one of a smaller number vested with certain powers, this obligation would be still stronger, and his acts subject to more severe scrutiny, and their validity determined by more rigid principles of morality, and freedom from motives of selfishness. All this falls far short, however, of holding that no such contract can be made which will be valid; and we entertain no doubt that the defendant in this case could make a loan of money to the company; and as we have already said that the evidence shows it to have been an honest transaction for the benefit of the corporation and its shareholders, both in the rate of interest and in the security taken, we think it was valid originally, whether liable to be avoided afterwards by the company or not.

If it be conceded that the contract by which the defendant became the creditor of the company was valid, we see no principle on which the subsequent purchase under the deed of trust is not equally so. The defendant was not here both seller and buyer. A trustee was interposed who made the sale, and who had the usual powers necessary to see that the sale was fairly conducted, and who in this respect was the trustee of the corporation, and must be supposed to have been selected by it for the exercise of this power. Defendant was at liberty to bid, subject to those rules of fairness which we have already conceded to belong to his peculiar position; for, if he could not bid, he would have been deprived of the only means which his contract gave him of making his debt out of the security on which he had loaned his money. We think the sale was a fair one. The company was hopelessly involved beside the debt to defendant. The well was exhausted, to all appearance. The machinery was of little use for any other purpose, and would not pay transportation. Most of the stockholders who now promote this suit refused to pay assessments on their shares to aid the company. Nothing was left to the defendant but to buy it in, as no one would bid the amount of his debt.

The next question to be decided is, whether, under the circum-

stances of this case, the complainant had a right to avoid this sale at the time this suit was brought.

(The learned justice answered this question in the negative "because plaintiff comes too late with the offer to avoid the sale.")

*Decree affirmed.*¹⁴

SEYMOUR v. SPRING FOREST CEMETERY ASSN.

1895. 144 N. Y. 333, 39 N. E. 365.¹⁵

APPEAL from judgment in plaintiff's favor entered upon the report of a referee. The action was for an accounting. The material facts sufficiently appear from the opinion.

FINCH, J.—* * *

But the further claim is made that, because Hotchkiss and Seymour were officers of the corporation, holding a fiduciary relation as trustees or directors, they could not lawfully buy the valid and outstanding obligations of the company at less than par and enforce them for the full amount against the debtors. If that be sound doctrine, as is stoutly maintained, if directors cannot in any case invest in the bonds of their own companies except at the peril of a constructive fraud, if they cannot safely buy such bonds below par, be-

* *Snediker v. Ayers* (1905) 146 Cal. 407, 80 Pac. 511; *Merrick v. Peru Coal Co.* (1871) 61 Ill. 472; *Harts v. Brown* (1875) 77 Ill. 226 (but see *Beach v. Miller* (1889) 130 Ill. 162, 22 N. E. 464, 17 Am. St. 291; *Higgins v. Lansingh* (1895) 154 Ill. 301, 40 N. E. 362); *McMurtry v. Montgomery etc. Temple Co.* (1887) 86 Ky. 206, 9 Ky. L. 541, 5 S. W. 570; *Saltmarsh v. Spaulding* (1888) 147 Mass. 224, 17 N. E. 316; *Lucas v. Friant* (1897) 111 Mich. 426, 69 N. W. 735; *Horbach v. Marsh* (1893) 37 Neb. 22, 55 N. W. 286 (director must affirmatively show good faith and payment of full value); *Preston v. Loughran* (1890) 58 Hun (N. Y.) 210, 12 N. Y. S. 313, 34 N. Y. St. 391 (but see *Hoyle v. Plattsburgh & c. R. Co.* (1873) 54 N. Y. 314, 13 Am. Rep. 595); *New Memphis Gaslight Co. Cases* (1900) 105 Tenn. 268, 60 S. W. 206, 80 Am. St. 880, *Accord*. In the last cited case, *Beard, J.*, said: "On this point there is some conflict of authority, but when it is once determined that a director may lend his credit in good faith to the corporation to enable it to carry on its legitimate business, and take as indemnity to secure himself from personal loss, its bonds, it seems to follow, necessarily, that he acquires the right, as any other mortgagee, to protect himself even to the extent of being a purchaser at a foreclosure sale, which has become inevitable through no fault or design of his."

Contra, *Covington etc. R. Co. v. Bowler's Heirs* (1872) 9 Bush (Ky.) 468; *McAllen v. Woodcock* (1875) 60 Mo. 174 (purchase by treasurer at sheriff's sale); *Metropolitan Elevated R. Co. v. Manhattan Elevated R. Co.* (1884) 11 Daly (N. Y.) 373, 14 Abb. N. C. (N. Y.) 103, *semble*.

See also *Fryer v. Wiedemann* (1912) 148 Ky. 379, 146 S. W. 752; *Janney v. Minneapolis Industrial Exposition* (1900) 79 Minn. 488, 82 N. W. 984, 50 L. R. A. 273 (purchase by directors at assignee's sale); *Union Trust Co. v. Carter* (1905) 139 Fed. 717.

Cf. Marr v. Marr (1907) 72 N. J. Eq. 797, 66 Atl. 182 (valuable discussion of authorities).—Eds.

* Statement abridged. Portion of opinion omitted.—Eds.

cause they deem them unduly depressed, if titles to corporate obligations passing through their hands become tainted by their touch, it is quite time that the courts should give, what they have not given, a very definite and distinct warning. Some citations of seeming authority are pressed upon us and others exist. The broad rule is stated in *Perry on Trusts* (§ 428), that "a trustee, executor or assignee cannot buy up a debt or incumbrance to which the trust estate is liable for less than is actually due thereon, and make a profit to himself," and that is the doctrine invoked in this case as applicable to a director regarded as a trustee of the corporation. But the statement, however correct in its application to specific instances, must be taken with the limitations which belong to it. Its foundation is that a fiduciary agent, owing a duty to his principal, cannot make a contract for his own benefit which is or may be inconsistent with that duty, and the cases generally are of two kinds. The trustee buys in the property of his principal at a sacrifice for his own benefit, when, if he bought it at all, it was his duty to do it for his principal, or he makes a contract in behalf of his principal with himself directly or indirectly as the other party to the agreement. The first class of cases is illustrated by *Slade v. Van Vechten* (11 Paige, 26), where the assignee bought in assigned property at a sheriff's sale and claimed the personal benefit of his bargain; and the second class by *Munson v. S. G. & C. R. R. Co.* (103 N. Y. 58), in which the directors contracting had a private and personal interest, possibly adverse to their fiduciary duty. Almost, if not quite all, of the cases cited by the learned counsel for the appellant belong to one or the other of these two classes. But they do not decide this case, for *Hotchkiss* and *Seymour* neither bought in any property of the company nor dealt with the corporation in any respect. They made their contract, not with it, but with third persons capable of protecting their own rights, and bought nothing which the corporation owned or to which it had a right. We must go to still other cases, founded it may be to some extent upon similar ideas of fiduciary duty, to discover even an approximate authority. There are cases of co-partnership in which the general rules pertaining to that specific relation might prove to be broad enough to cover the purchase of the debt owing by the firm, (*Am. Bk. Note Co. v. Edson*, 56 Barb. 89), and other cases in which the duties flowing from a liquidation conducted by the trustee, and as to which he owes a specific trust duty, forbid a purchase by the trustee for his own benefit at a discount. But in every class of cases the rule is founded upon the unwillingness of the law to uphold contracts which bring into collision the trust duty and the personal interest, and it is because of that collision, and the temptations which surround it, that it declares the contract voidable at the election of the beneficiary without investigating the good or bad faith of the trustee. The entire basis of the rule consists in this collision between trust duty and personal interest, and the equitable prohibition has no application where there is no such possible inconsistency. There is no

such conflict in the ordinary case of the purchase by a director in a going corporation of its outstanding obligations. There is no present duty resting upon him to extinguish them. The time for that has not come, the duty has not arisen, may never arise, the corporation is not prepared to pay, does not contemplate paying, but intends and expects to await the full maturity of the debt. Unless some special fund has been provided, or some special liquidation has been ordered, the director owes no duty to his company to discharge or buy in the outstanding bonds, and may purchase for himself because no inconsistent trust duty has arisen. Why should he not? While the bonds are running to their maturity, and the corporation is not able to extinguish them, is not bound to do so, does not even wish or seek to do so, what does it matter who holds the securities or on what terms they pass from hand to hand? It seems to me that we are asked to crowd the rule almost to the verge of an absurdity, and to inflict a vital injury upon business interests by tainting with invalidity the holding by a director of the unmatured obligations of the corporation bought by him in the open market and not put in liquidation or sought to be extinguished. There must at least be some fact or circumstance which charges the trustee with a present duty to act for his company in respect to the bonds, which duty is or may be inconsistent with a personal purchase. No such duty rested upon Hotchkiss and Seymour, and they had a right to buy and hold for their own benefit.

Indeed, there is a further and equally conclusive answer. **[I**f the doctrine invoked applied to this case it would make the purchase not void but voidable at the election of the corporation, and that election must be made promptly and upon sufficient knowledge of the facts. The beneficiary cannot wait and speculate upon the chances of delay, but must act. Here the purchase was made before 1873, and in 1880 the corporation is found recognizing and ratifying the title of the vendees or their successors, making payments to them, and providing for future payments, and it is only after a delay of fifteen years that an attempt to repudiate the purchase is made. * * *

(The learned judge then *held* that "it is too late now to question the title of the trustees.")

*Judgment affirmed.*¹⁶

¹⁶ In *Camden etc. Trust Co. v. Citizens' etc. Storage Co.* (1905) 69 N. J. Eq. 718, 61 Atl. 529 (aff'd., 65 Atl. 980), *held* that a director might purchase corporate bonds at their market value from a holder thereof and enforce them subsequently against the corporation at their full face value. *Bergen, V. C.*, said: "It is also insisted that as Furbush purchased the bonds for less than their face value, Brown, being a director, ought not now to recover more than the amount paid by Furbush, but there is nothing in the case to justify such a result, for the bonds were not, owing to the character of the business the company was engaged in, readily marketable. Efforts had been made to sell to other parties, and after failure to find another purchaser, Furbush bought them at a price which cannot be said to have been unconscionable in view of all the circumstances, and unless fraud be shown or some unjust advantage taken of a situation, there is no reason why the

LANDES v. HART.

1909. 131 App. Div. (N. Y.) 6, 115 N. Y. S. 337.

APPEAL by the defendants, Patrick A. Hart and another, from a judgment of the Supreme Court in favor of the plaintiff, entered in the office of the clerk of the county of New York on the 17th day of March, 1908, upon the verdict of a jury, and also from an order entered in said clerk's office on the 26th day of March, 1908, denying the defendants' motion for a new trial made upon the minutes.

HOUGHTON, J.—The plaintiff was a director of the Baltic Land and Improvement Company which owned a tract of land requiring extensive grading, laying out of streets and sewerage for building purposes. Negotiations were entered into with the defendants for doing such work, and resulted in a contract therefor amounting to upwards of \$10,000. Plaintiff previous to making the contract had had interviews with defendants respecting such contract and claims that defendants promised to pay him at least \$500 if he should procure for them the contract for the work from his corporation. The plaintiff recommended to his board of directors that the contract be let to the defendants and put the motion to that effect, and voted that the resolution be adopted. The defendants entered upon the prosecution of the work and at the time of the commencement of the action had received certain of the stipulated partial payments.

The learned trial court submitted the case to the jury on the theory that the plaintiff's claim was valid provided he disclosed to his codirectors his alleged bargain with the defendants. Some of the directors testified that they knew about it and others that they did not; but the plaintiff testified that a majority of his codirectors had been told of his arrangement with the defendants and made no objection.

Whether the plaintiff's codirectors knew of his pretended arrangement with the defendants or not, upon his own showing his contract was illegal and void as against public policy, and his complaint should have been dismissed. Holding the office of director of the contracting corporation he occupied a fiduciary relation to it and was a trustee for it and its stockholders and creditors. [As such trustee it was his duty to obtain as low a price as he was able from the defendants for the doing of the contemplated work. If the defendants could afford to pay the plaintiff \$500 from the amount which they were to receive from the corporation for the work, they could afford to make a contract to do it for \$500 less than the stipulated price, and

officers of a company may not purchase its bonds at their market value." (p. 723)

See also *Higgins v. Lansingh* (1895) 154 Ill. 301, 40 N. E. 362; *McIntyre v. Ajax Min. Co.* (1904) 28 Utah 162, 77 Pac. 613 (citing and following the principal case). Cf. *James v. Railroad Co.* (1867) 6 Wall. (U. S.) 752, 18 L. ed. 885.

But see 10 Cyc. 798.—Eds.

it was plaintiff's duty as director to obtain for his corporation the contract at such reduced amount. The effect of the arrangement which plaintiff claims he had with the defendants was to make a bargain with them to violate his duty towards his corporation. An agreement which is designed, or which in its nature and effect tends to lead persons who are charged with the performance of trusts or duties for the benefit of others to violate or betray them, is contrary to public policy and void and cannot be enforced. (Bliss v. Matteson, 52 Barb. 335; *affd.*, 45 N. Y. 22; Moss v. Cohen, 11 Misc. Rep. 184; West v. Camden, 135 U. S. 507; Barkley v. Williams, 26 Ill. App. 213.) Such a contract with a third person is not made valid although the acts of the unfaithful agent may have in fact resulted in benefit to his principal (Lum v. McEwen, 56 Minn. 278); nor by the fact that the unfaithful director of a corporation informed his codirectors of his corrupt bargain. (Munson v. S. G. & C. R. R. Co., 103 N. Y. 59, 74.)

Objection is made that the defendants' answer contains only a general denial and that the illegality of the contract must be affirmatively pleaded. Where from the plaintiff's own proof a contract is shown to be void as contrary to public policy a general denial is sufficient. (Auerbach v. Curie, 119 App. Div. 175.)

The contract which plaintiff proved was not only bad in morals but bad in law, and the judgment must be reversed. There is no possibility of his proving a good contract on a new trial and the complaint should be dismissed.

The judgment and order should be reversed, with costs, and the complaint dismissed, with costs.

INGRAHAM, P. J., McLAUGHLIN, CLARKE and SCOTT, JJ., concurred.

*Judgment and order reversed and complaint dismissed, with costs.*¹⁷

¹⁷ See also, Liquidators of Imperial Mercantile Credit Assn. v. Coleman (1873) L. R. 6 Eng. & Ir. App. Cas. 189; Hoffman v. Reichert (1893) 147 Ill. 274, 35 N. E. 527, 37 Am. Rep. 219; Klein v. Independent Brewing Assn. (1908) 231 Ill. 594, 83 N. E. 434; Bent v. Priest (1881) 10 Mo. App. 543; Redhead v. Parkway Driving Club (1896) 148 N. Y. 471, 42 N. E. 1047 (stockholder acting as member of a purchasing committee cannot make a profit for his firm); McClure v. Law (1899) 161 N. Y. 78, 55 N. E. 388, 76 Am. St. 262 (secret profit by president); Asphalt Const. Co. v. Bouker (1912) 135 N. Y. S. 714 (directors jointly and severally liable to account to the corporation for secret profits; but see note, 12 Columbia Law Rev. 644); Ryan v. Grissinger (1912) 136 N. Y. S. 134; Koehler v. Black River etc. Iron Co. (1862) 2 Black (U. S.) 715, 17 L. ed. 339.

In Parker v. Nickerson (1873) 112 Mass. 195, directors purchased a steam vessel in their individual capacities. Subsequently, as directors of the company and acting on its behalf, they purchased the vessel from themselves at a very great advance. *Held*, the directors must account to the receivers of the corporation for "all the profits thus made."—Eds.

V
Section 4—Relation to Stockholders Individually.

BOARD OF COMMISSIONERS v. REYNOLDS.

1873. 44 Ind. 509.¹

FROM the White Circuit Court.

WORDEN, J.— * * *

The facts in the case as alleged are, in substance, as follows:

The county of Tippecanoe was the owner of five hundred and seventy paid up shares of the capital stock of the Lafayette and Indianapolis Railroad Company, of fifty dollars each amounting to twenty-eight thousand five hundred dollars; that on June 24th, 1865, the total amount of the stock of the company was only two hundred and fifty thousand dollars; that the road had been built mainly from the proceeds of bonds sold, and had, by its earnings, paid off the bonded debt, and also, that the floating debt was paid, or means accumulated and on hand with which to pay it; that the stock owned by the county was, at that time, worth three hundred and forty-two thousand dollars; that the defendant was the president of the company and the principal manager of its affairs; that the condition of the company had been concealed by the defendant, by failing to declare dividends, and by representations that the stock was not worth its face, and by failing to show the condition of the affairs of the company; that the plaintiffs were ignorant of the value of the stock, which the defendant knew; that he represented that the depreciation of the value of the stock had been caused by losses sustained by the company, when he knew that the accumulations of the company were sufficient to pay all debts and losses and leave the stock eleven hundred per cent. above par; that, under these circumstances, the defendant, through his agent, Moses Fowler, who was also a director of the company, purchased the stock of the county, on said 24th day of June, 1865, for the sum of twenty-five thousand six hundred and fifty dollars, being ninety cents on the dollar, and had it transferred to one Wilson, to hold as his trustee; that the defendant was then negotiating to sell the road to the Indianapolis and Cincinnati Railroad Company, and afterward did sell it for two million five hundred thousand dollars, secured by first mortgage bonds on the road from Lafayette to Indianapolis, with a further lien on the Indianapolis and Cincinnati road.

Prayer for judgment for three hundred and fifteen thousand three hundred and fifty dollars, in different forms, and for general relief. * * *

We have carefully considered the evidence in the cause and are satisfied that no actual fraud was established in the purchase of the stock by the defendant from the plaintiff. The defend-

¹ Statement abridged. Portions of opinion omitted.—Eds.

ant, doubtless, knew much more about the condition of the affairs of the company and the value of the stock, both present and prospective, than the plaintiff. He purchased the stock greatly below its real value, as subsequent events established, but he paid the market value, at the time, so far as it seems to have had a market value. Had the defendant not been connected with the company as one of its officers, there is nothing in the case that would furnish any reasonable ground to claim that the purchase was, in any manner, infected with fraud. It is not shown by the evidence that there was any special trust or confidence reposed in the defendant by the plaintiff, which was violated by the former, or of which he took advantage. These are the conclusions at which we arrive from the evidence, which is quite voluminous and cannot be set out without extending this opinion to an inadmissible length. It is very clear, according to the well established practice of the court, that we cannot disturb the finding of the court below on the ground of actual fraud. Some other element must enter into the case, in order to justify us in disturbing the finding. This brings us to the question which has been chiefly argued by counsel, viz.: Was the defendant, in consequence of being a director and the president of the company, a trustee of the plaintiff as a stockholder, whereby it became his duty, as a purchaser of the stock, to pay a fair and adequate price for it, to take no advantage of the relation which he bore to the company or the knowledge acquired thereby, and to disclose to the plaintiff all the material facts within his knowledge, not known to the plaintiff, affecting the value of the stock?

We are of opinion, upon an examination of such authorities as have been brought to our notice, upon the point, that the relation of trustee and cestui que trust does not exist in such case. It is said very frequently in the books that the directors of a corporation are trustees of the stockholders, and that the relation of trustee and cestui que trust, with its consequences, exists between them. But these expressions must always be understood to have relation to the cases to which they are applied, and not to be of universal application. It may be conceded that, in respect to the property of the corporation, whether it be land, money, securities, capital stock, or other property held by the corporation, and the management of its business, the directors are trustees for the stockholders. The action of the directors in respect to the property of the corporation must affect, to a greater or less degree, the stockholders generally. It has been generally in such cases, or where the action of the directors has affected the whole body of stockholders, that the relation of trustee and cestui que trust has been held to exist. In a late case in Pennsylvania, *Spering's Appeal*, 71 Penn. St. 11, 20, *SHARSWOOD, J.*, in delivering the opinion of the court, says: "It is by no means a well settled point what is the precise relation which directors sustain to stockholders. They are undoubtedly said in many authorities to be trustees, but that as I apprehend is only in a general sense, as we

term an agent or any bailee intrusted with the care and management of the property of another. It is certain that they are not technical trustees."

To show the diversity of language employed in different cases and the necessity of keeping in view the case to which it is applied, we make a short extract from the case of *Smith v. Hurd*, 12 Met. 371. It was an action on the case at common law, brought by an individual holder of shares in an incorporated bank against the directors, setting forth various acts of negligence and malfeasance through a series of years, in consequence of which, as the declaration alleged, the whole capital of the bank was wasted and lost, and the shares of the plaintiff became of no value.

SHAW, C. J., in delivering the opinion of the court, said: "There is no legal privity, relation, or immediate connection, between the holders of shares in a bank, in their individual capacity, on the one side, and the directors of the bank on the other. The directors are not the bailees, the factors, agents or trustees of such individual stockholders." It was held that the action could not be maintained.

A similar decision was made in the case of *Allen v. Curtis*, 26 Conn. 456. ELLSWORTH, J., in pronouncing the decision of the court, said: "Besides, the directors of the bank are the agents of the bank. The bank is the only principal, and there is no such trust for, or relation to, a stockholder as has been claimed by the plaintiff. The entire duty of the directors, growing out of their agency, is owed to the bank, which, under the charter is the sole representative of the stockholders, and the legal protector and defender of their property."

It seems to us, however, keeping in view the current of authorities, that notwithstanding the general language employed in the above cases, for some purposes, the directors of a corporation stand in a relation similar to that of trustees for the shareholders. This seems to be the case in reference to the management, by the directors, of the property and general affairs of the corporation. These are matters usually entrusted to the directors, and in respect to which they are empowered to act; and their action affects the whole body of shareholders, beneficially or injuriously, in respect to dividends upon, or the value of, their stock.

But stock in a corporation held by an individual is his own private property, which he may sell or dispose of as he sees proper, and over which neither the corporation nor its officers have any control. It is the subject of daily commerce and is bought and sold in market like any other marketable commodity. The directors have no control or dominion over it whatever or duty to discharge in reference to its sale and transfer, unless it be to see that proper books and facilities are furnished for that purpose. As the property of the individual holder, he holds it as free from the dominion and control of the directors, as he does his lands or other property. This view is very well illustrated by what was said in the case of *Van Allen v. The Assessors*, 3 Wall. 573, in which it was held that shares in the national

banks might be taxed by the states. Mr. Justice Nelson in delivering the opinion of the court, p. 583, said: "But, in addition to this view, the tax on the shares is not a tax on the capital of the bank. The corporation is the legal owner of all the property of the bank, real and personal; and within the powers conferred upon it by the charter, and for the purposes for which it was created, can deal with the corporate property as absolutely as a private individual can deal with his own. This is familiar law, and will be found in every work that may be opened on the subject of corporations. A striking exemplification may be seen in the case of *The Queen v. Arnaud*, 9 A. & E., N. S. 806. The question related to the registry of a ship owned by a corporation. Lord Denman observed: 'It appears to me that the British corporation is, as such, the sole owner of the ship. The individual members of the corporation are no doubt interested in one sense in the property of the corporation, as they may derive individual benefits from its increase, or loss from its decrease; but in no legal sense are the individual members the owners.'

"The interest of the shareholder entitles him to participate in the net profits earned by the bank in the employment of its capital, during the existence of its charter, in proportion to the number of his shares; and, upon its dissolution or termination, to his proportion of the property that may remain of the corporation after the payment of its debts. This is a distinct independent interest or property, held by the shareholder like any other property that may belong to him. Now, it is this interest which the act of Congress has left subject to taxation by the states," etc.

Such being the nature of the interest of the stockholder in his stock, and the directors having no control, power, or dominion over it or duty to discharge in reference to it, beyond the duty devolving upon them to prudently manage the affairs and property of the corporation itself, it seems to us to be very clear, that, in the purchase of stock by a director from the holder, the relation of trustee and *cestui que trust* does not exist between them.

The case of *Carpenter v. Danforth*, 52 Barb. 581, a very well considered case, is directly in point. There, Danforth, who was one of the trustees or directors of the corporation, purchased of the plaintiff one hundred and thirty-six shares of the stock of the National Bank Note Company, and the purpose of the action was to have the sale declared void, and to have the plaintiff restored to the rights and interests which he would have had if the sale had not been made upon the ground of fraud and undue influence. It was held that the relation of trustee and *cestui que trust* did not exist.

Many cases have been cited, in which it has been said that the directors of a corporation are trustees for the stockholders, but it has been said generally, if not always, with reference to the management, by the directors, of the property or business of the corporation itself. We proceed to notice the cases. * * *

We have thus noticed all the cases that have been cited upon the

question involved. None of them conflict with that of *Carpenter v. Danforth*, supra, or with the conclusion at which we have arrived as hereinbefore stated. They are all cases in which the acts of the directors, in respect to which they were held to be trustees of the stockholders, had relation to the property or to the business of the corporation. Such is not the case here.

The judgment below is *affirmed*, with costs.

DOWNNEY, C. J.—In my opinion, the evidence in the record in this case shows that the appellee was guilty of actual fraud in his purchase of the stock of the county in the railroad of which he was a director and the president.

If this were not so, I am clearly of the opinion that he occupied a relation of trust and confidence toward the county, which, under the circumstances disclosed, made him guilty of constructive fraud.

I regard the contract obtained from the county commissioners by the appellee as hard, unconscionable, and fraudulent in either view of it, and am therefore of the opinion that the judgment of the circuit court should be reversed.

*Petition for a rehearing overruled.*²

² *Hooker v. Midland Steel Co.* (1905) 215 Ill. 444, 74 N. E. 445, 106 Am. St. 170; *Bawden v. Taylor* (1912) 254 Ill. 464, 98 N. E. 941 ("Officers of a corporation may purchase the stock of stockholders on the same terms and as freely as they might purchase of a stranger"); *Walsh v. Goulden* (1902) 130 Mich. 531, 90 N. W. 406; *Carpenter v. Danforth* (1868) 52 Barb. (N. Y.) 581, esp. p. 584; *Deaderick v. Wilson* (1874) 8 Baxt. (67 Tenn.) 108; *O'Neile v. Ternes* (1903) 32 Wash. 528, 73 Pac. 692; *Grant v. Attrill* (1882) 11 Fed. 469; *Percival v. Wright* (1902) 2 Ch. Div. 421 ("directors not trustees for the individual shareholders"), *Accord*.

In the case first cited, Cartwright, J., said (pp. 450-451): "It is contended that Beatty, being the president and director of the Midland Steel Company, was a trustee for the complainant as a stockholder, and was therefore in a fiduciary and confidential relation requiring him to disclose all such facts within his knowledge, and that he could not retain a benefit acquired by a breach of that duty or use knowledge in his possession to obtain a bargain from the complainant. The management of the business and property of a corporation is entrusted to its officers, and they are empowered to act for the whole body of stockholders. They therefore occupy the position of trustees for the stockholders as a body in respect to such business and property, and cannot have or acquire any personal or pecuniary interest in conflict with their duty as such trustees. A director, however, does not sustain that relation to an individual stockholder with respect to his stock, over which he has no control whatever, but he may deal with an individual stockholder and purchase his stock practically on the same terms as a stranger. In the absence of actual fraud such a purchase will not be set aside for a mere failure to disclose any information the director may have affecting the value of the stock."

See *Allen v. Curtis* (1857) 26 Conn. 456; *Perry v. Pearson* (1890) 135 Ill. 218, 25 N. E. 636; *Smith v. Hurd* (1847) 12 Metc. (Mass.) 371, 46 Am. Dec. 690; *Rafferty v. Donnelly* (1900) 197 Pa. St. 423, 47 Atl. 202.—Eds.

STRONG v. REPIDE.

1908. 213 U. S. 419, 53 L. ed. 853.*

THIS action was commenced on the twelfth day of January, 1904, in the Court of First Instance of the city of Manila, Philippine Islands, by the plaintiffs in error, Eleanor Erica Strong and Richard P. Strong, her husband, against the defendant in error. It was brought by the plaintiff, Mrs. Strong, as the owner of eight hundred shares of the capital stock of the Philippine Sugar Estates Development Company, Limited, (the other plaintiff being added as her husband), to recover such shares from defendant (who was already the owner of 30,400 of the 42,030 shares issued by the company), on the ground that the shares had been sold and delivered by plaintiff's agent to the agent of defendant, without authority from plaintiff; and also on the ground that defendant fraudulently concealed from plaintiff's agent, one F. Stuart Jones, facts affecting the value of the stock so sold and delivered. The stock was of the par value of \$100 per share, Mexican currency.

The plaintiff never had any negotiations for the sale of the stock herself; and was ignorant that it was sold until some time after the sale, the negotiations for which took place between an agent of the plaintiff and an agent of defendant, the name of the defendant being undisclosed.

In addition to his ownership of almost three-fourths of the shares of the stock of the company, the defendant was one of the five directors of the company, and was elected by the board the agent and administrator general of such company, "with exclusive intervention in the management" of its general business.

MR. JUSTICE PECKHAM, after making the foregoing statement, delivered the opinion of the court. * * *

The question in this case, therefore, is whether, under the circumstances above set forth, it was the duty of the defendant, acting in good faith, to disclose to the agent of the plaintiff the facts bearing upon or which might affect the value of the stock.

If it were conceded, for the purpose of the argument, that the ordinary relations between directors and shareholders in a business corporation are not of such a fiduciary nature as to make it the duty of a director to disclose to a shareholder the general knowledge which he may possess regarding the value of the shares of the company before he purchases any from a shareholder, yet there are cases where, by reason of the special facts, such duty exists. The supreme courts of Kansas and of Georgia have held the relationship existed in the cases before those courts because of the special facts which took them out of the general rule, and that under those facts the director could not purchase from the shareholder his shares without

* Statement abridged. Portions of opinions omitted.—Eds.

informing him of the facts which affected their value. *Stewart v. Harris*, 69 Kansas, 498, 77 Pac. 277; *Oliver v. Oliver*, 118 Georgia, 362, 45 S. E. 232. The case before us is of the same general character. On the other hand there is the case of *Board of Commissioners v. Reynolds*, 44 Indiana, 509-515, where it was held (after referring to cases) that no relationship of a fiduciary nature exists between a director and a shareholder in a business corporation. Other cases are cited to that effect by counsel for defendant in error. These cases involved only the bare relationship between director and shareholder. It is here sought to make defendant responsible for his actions, not alone and simply in his character as a director, but because, in consideration of all the existing circumstances above detailed, it became the duty of the defendant, acting in good faith, to state the facts before making the purchase. That the defendant was a director of the corporation is but one of the facts upon which the liability is asserted, the existence of all the others in addition making such a combination as rendered it the plain duty of the defendant to speak. He was not only a director, but he owned three-fourths of the shares of its stock, and was, at the time of the purchase of the stock, administrator general of the company, with large powers, and engaged in the negotiations which finally led to the sale of the company's lands (together with all the other friar lands) to the Government at a price which very greatly enhanced the value of the stock. He was the chief negotiator for the sale of all the lands, and was acting substantially as the agent of the shareholders of his company by reason of his ownership of the shares of stock in the corporation and by the acquiescence of all the other shareholders, and the negotiations were for the sale of the whole of the property of the company. By reason of such ownership and agency, and his participation as such owner and agent in the negotiations then going on, no one knew as well as he the exact condition of such negotiations. No one knew as well as he the probability of the sale of the lands to the Government. No one knew as well as he the probable price that might be obtained on such sale. The lands were the only valuable asset owned by the company. Under these circumstances and before the negotiations for the sale were completed the defendant employs an agent to purchase the stock, and conceals from the plaintiff's agent his own identity and his knowledge of the state of the negotiations and their probable result, with which he was familiar as the agent of the shareholders and much of which knowledge he obtained while acting as such agent and by reason thereof. The inference is inevitable that at this time he had concluded to press the negotiations for a sale of the lands to a successful conclusion, else why would he desire to purchase more shares which, if no sale went through, were in his opinion, worthless, because of the failure of the Government to properly protect the lands in the hands of their then owners? The agent of the plaintiff was ignorant in regard to the state of the

negotiations for the sale of the land, which negotiations and their probable result were a most material fact affecting the value of the shares of stock of the company, and he would not have sold them at the price he did had he known the actual state of the negotiations as to the lands and that it was the defendant who was seeking to purchase the stock. Concealing his identity when procuring the purchase of the stock, by his agent, was in itself strong evidence of fraud on the part of the defendant. Why did he not ask Jones, who occupied an adjoining office, if he would sell? But by concealing his identity he could by such means the more easily avoid any questions relative to the negotiations for the sale of the lands and their probable result, and could also avoid any actual misrepresentations on that subject, which he evidently thought were necessary in his case to constitute a fraud. He kept up the concealment as long as he could, by giving the check of a third person for the purchase money. Evidence that he did so was objected to on the ground that it could not possibly even tend to prove that the prior consent to sell had been procured by the subsequent check given in payment. That was not its purpose. Of course, the giving of the check could not have induced the prior consent, but it was proper evidence as tending to show that the concealment of identity was not a mere inadvertent omission, an omission without any fraudulent or deceitful intent, but was a studied and intentional omission to be characterized as part of the deceitful machinations to obtain the purchase without giving any information whatever as to the state and probable result of the negotiations, to the vendor of the stock, and to in that way obtain the same at a lower price. After the purchase of the stock he continued his negotiations for the sale of the lands, and finally, he says, as administrator general of the company, under the special authority of the shareholders, and as attorney in fact he entered into the contract of sale December 21, 1903. The whole transaction gives conclusive evidence of the overwhelming influence defendant had in the course of the negotiations as owner of a majority of the stock and as agent for the other owners, and it is clear that the final consummation was in his hands at all times. [If under all these facts he purchased the stock from the plaintiff, the law would indeed be impotent if the sale could not be set aside or the defendant cast in damages for his fraud.]

The Supreme Court of the islands, in holding that there was no fraud in the purchase, said that the responsibility of the directors of a corporation to the individual stockholders [did not extend beyond the corporate property actually under the control of the directors; that they did not owe any duty to the members in respect to their individual stock, which would prevent them from purchasing the same in the usual manner.] While this may in general be true, we think it is not an accurate statement of the case, regard being had to the facts above mentioned.

It is said that by the code of commerce of the Philippine Islands

the directors are declared to be mandatories of the society, and that by article 1459 of the Spanish Civil Code they are prohibited from acquiring by purchase, even at public or judicial auction, the property the administration or sale of which may have been entrusted to them, and that this is the extent of the prohibition. This provision has no reference to the purchase for himself, under such facts as existed here, by an officer of a corporation, of stock in the corporation owned by another. The case before us seems a plain one for holding that, under the circumstances detailed, there was a legal obligation on the part of the defendant to make these disclosures. * * *

Other objections made by the defendant's counsel we have examined, but do not regard them as important. We therefore reverse the judgment of the Supreme Court, dismissing the complaint and affirm that of the Court of First Instance, and

*It is so ordered.*⁴

⁴In *Oliver v. Oliver* (1903) 118 Ga. 362, 45 S. E. 232, *held* that where a president and director of a corporation purchases its stock from shareholders at \$110 per share, studiously concealing the circumstance that negotiations for the sale of the company's properties are being consummated, which would make the stock worth \$185 per share, the shareholders are entitled to a rescission of the sale of their stock. The court, speaking by Lamar, J. (now Mr. Justice Lamar) said: "No process of reasoning and no amount of argument can destroy the fact that the director is, in a most important and legitimate sense, trustee for the stockholder. *Jackson v. Ludeling*, 21 Wall. 616; 2 Pom. Eq. Jur. (2d ed.) § 1090. Not a strict trustee, since he does not hold title to the shares; not even a strict trustee who is practically prohibited from dealing with his *cestui que trust*; but a quasi trustee as to the shareholder's interest in the shares. If the market or contract price of the stock should be different from the book value, he would be under no legal obligation to call special attention to that fact; for the stockholder is entitled to examine the books, and this source of information, at least theoretically, is equally accessible to both. It might be that the director is in possession of information which his duty to the company requires him to keep secret; and if so, he must not disclose the fact even to the shareholder; for his obligation to the company overrides that to an individual holder of the stock. But if the fact so known to the director cannot be published, it does not follow that he may use it to his own advantage, and to the disadvantage of one whom he also represents. The very fact that he cannot disclose prevents him from dealing with one who does not know, and to whom material information cannot be made known. If, however, the fact within the knowledge of the director is of a character calculated to affect the selling price, and can, without detriment to the interest of the company, be imparted to the shareholder, the director, before he buys, is bound to make a full disclosure. In a certain sense the information is a quasi asset of the company, and the shareholder is as much entitled to the advantage of that sort of an asset as to any other regularly entered on the list of the company's holdings. If the officer should purposely conceal from a stockholder information as to the existence of valuable property belonging to the company, and take advantage of this concealment, the sale would necessarily be set aside." (pp. 367-8).

In *Stewart v. Harris* (1904) 69 Kansas 498, 77 Pac. 277, 66 L. R. A. 261, 105 Am. St. 178, *Oliver v. Oliver*, (1903) 118 Ga. 362, 45 S. E. 232, is followed and *Atkinson, J.*, in *repudiating Board of Commissioners v. Reynolds*, 44 Ind. 509, said: "The rule laid down has met with much criticism. The posi-

tion taken leaves the stockholders' interest in the corporation and all matters affecting its value wholly in the charge and keeping of the managing officers of the corporation, and leaves the stockholders their legitimate prey. We cannot give the sanction of our approval to the views there expressed." But see, *contra*, *Crowell v. Jackson* (1891) 53 N. J. L. 656, 23 Atl. 426.

See also note, 17 *Harvard Law Rev.* 58; and article by H. L. Wilgus in 8 *Michigan Law Rev.* 267.—Eds.

CHAPTER VIII.

STOCKHOLDERS.

Section 1.—Right to Vote—The Voting Trust.

CAMDEN AND ATLANTIC R. R. Co. v. ELKINS.

1883. 37 N. J. Eq. 273.¹

ON APPEAL from a decree advised by Vice-Chancellor Van Fleet, whose opinion is reported in *Elkins v. Camden and Atlantic R. R. Co.*, 9 Stew. Eq. 467.

The opinion of the court was delivered by DEPUE, J.

The complainant's bill is purely an injunction bill. It prayed an injunction to restrain the directors from making any change in the by-laws, and forbidding the postponement of the election for directors. * * *

Contn. The appellants urge the retention of the appeal on the ground that the complainant is not a *bona fide* holder of stock of the corporation. They insist that he became the purchaser of the stock he holds with the money of rival companies, and that he holds it in the interest of those companies, and contemplates the use of it for the purpose of controlling the business of the corporation for the advantage of those other companies. They insist that therefore he has no standing in a court of equity to seek its aid in accomplishing his purposes.

The complainant appears, on the company's books, to be the owner of thirteen hundred and fifty shares of its capital stock, being more than a majority of its entire capital stock, and the stock he holds was regularly issued by the company and was regularly transferred to the complainant on the company's books. The statute makes the stock of a corporation personal property, and transferable on the books of the corporation. It vests in the stockholders the right to elect directors, who shall manage the business of the corporation for them. It secures to each stockholder the right to one vote, at every election of directors, for each share of the capital stock of the company held by him, and makes the books of the corporation plenary and conclusive evidence of the ownership¹ of stock and of the right to vote in virtue of such ownership. The right to hold elections for the directors of a corporation, and to vote at such

¹ A portion of the opinion omitted.—Eds.

elections, is a right that is inherent in the ownership of stock; and a stockholder who appears by the books to be such cannot be deprived of these rights upon the allegation that he proposes to use his legal rights for purposes which others may think to be detrimental to the interests of the corporation. *Pender v. Lushington*, L. R. 6 Ch. Div. 70. If the complainant, in virtue of his ownership of a majority of the stock, elected a board of directors of his own selection, and they should endeavor to misuse the franchise of the corporation, or improperly manage its affairs in the interest of other companies, to the prejudice of its stockholders as a class, the remedy is by proceedings by the attorney-general as the representative of the public, or by other stockholders whose rights may be injured by the unlawful acts of the directors. The directors who are in office, and who are the mere ministerial agents of the corporation, cannot dispute the right of stockholders to obtain a new election of directors, and prolong their own authority, on the ground that the proposed election is a step toward the illegal and improper control of the property or the business of the corporation. When that event occurs, or is impending, the proper means to redress or avert the wrong is in other parties and by other proceedings.

*Appeal unanimously dismissed.*²

² *Memphis &c. R. Co. v. Wood* (1889) 88 Ala. 630, 7 So. 108, 7 L. R. A. 605, 16 Am. St. 81, *Contra*. But see *Oelbermann v. N. Y. &c. R. Co.* (1894) 76 Hun 613, 77 Hun (N. Y.) 332, 29 N. Y. S. 545, 59 N. Y. St. 881, 60 N. Y. St. 876 (railroad company purchasing stock in another company has the same voting rights as any other shareholder); *Rogers v. Nashville &c. R. Co.* (1898) 91 Fed. 299, 33 C. C. A. 517. *Cf.* *Dunbar v. American &c. Telegraph Co.* (1906) 224 Ill. 9, 79 N. E. 423, 115 Am. St. 132.

In *Bjorngaard v. Goodhue County Bank* (1892) 49 Minn. 483, 52 N. W. 48, *held*, "Stockholders in a corporation are not disqualified to vote upon a matter coming before a stockholders' meeting by the fact that they may have a personal interest in the matter, as upon a proposition to ratify a purchase of property from themselves which they as directors had assumed to make." So also, *Blinn v. Riggs* (1903) 110 Ill. App. 37, (affirmed 208 Ill. 473, 70 N. E. 704, 100 Am. St. 234.)

In *Lord v. Equitable Life Assur. Society* (1909) 194 N. Y. 212, at p. 228, 87 N. E. 443, at p. 448, 22 L. R. A. (N. S.) 420n, Vann, J. said: "The right to vote for directors, therefore, is the right to protect property from loss and make it effective in earning dividends. In other words, it is the right which gives the property value and is part of the property itself, for it cannot be separated therefrom. Unless the stockholder can protect his investment in this way he cannot protect it at all, and his property might be wasted by feeble administration and he could not prevent it. He might see the value of all he possessed fading away, yet he would have no power, direct or indirect, to save himself, or the company from financial downfall. With the right to vote, as we may assume, his property is safe and valuable. Without that right, as we may further assume, his property is not safe and may become of no value. To absolutely deprive him of the right to vote, therefore, is to deprive him of an essential attribute of his property."

According to the old common-law rule each shareholder was entitled only to one vote without regard to the number of shares he owned. *Taylor v. Griswold* (1834) 2 Gr. (14 N. J. L.) 222, at page 237; *In re Horbury Bridge &c. Co.* (1879) L. R. 11 Ch. Div. 109. This rule has been generally abrogated by statute.—Eds.

COMMONWEALTH EX REL. EBERHARDT v. DALZELL.

1893. 152 Pa. St. 217, 25 Atl. 535.*

PETITION for alternative writ of quo warranto, to determine whether J. H. Dalzell, C.-L. Magee, Joshua Rhodes, George B. Hill and Fred Gwinner were entitled to act as directors of the Pittsburgh, Allegheny & Manchester Traction Company.

From the petition it appeared that at a meeting of the stockholders of the said company held on May 16, 1892, the five respondents were declared elected to the position of directors. One of the candidates for the office of director was the relator, William Eberhardt, who, by proxies under seal, claimed the right to vote stock, held by Watson and Wood as trustees, and so registered in the stock book of the corporation. The votes were rejected. If they had been received relator would have had more votes than defendants. Further facts appear by the opinion of the Supreme Court.

The case was heard upon petition setting out these facts and demurrer to answer. The answer denied the right to vote the stock in question. The court overruled the demurrer, and entered judgment for defendants, in an opinion by Ewing, P. J., 1 Dist. R. 657.

OPINION BY MR. JUSTICE MITCHELL, January 3, 1893.

The right of voting stock at corporate elections is an incident of ownership, to be exercised, of course, in the mode and under the restrictions prescribed by the charter and by-laws; but nevertheless a part of the stockholder's property, inherent in him by virtue of his title. As said by the present Chief Justice in *Tunis v. Hestonville R. W. Co.*, 30 W. N. 96, "the right of voting stock is inseparable from the right of ownership. The one follows as a sequence from the other, and the right to vote cannot be separated from the ownership without the consent of the legal owner." But though the person who votes must be an owner, "it does not follow that he must be the only one. If, for instance, stock is pledged as a collateral, whether the debtor or creditor shall vote depends on the terms on which the pledge is made. The power is, under these circumstances, necessarily to some extent severed from the ownership, and the parties may consequently determine on which side it shall lie;" *Hare, P. J., Shelmerdine v. Welsh*, 47 Leg. Int. 26. In the absence of any agreement between the parties on this point, it would seem that the right to vote should follow the legal title. If that was allowed to remain in the pledgor his right to vote could not be questioned, while, on the other hand, if the legal title was transferred to the pledgee, his prima facie right would be equally clear. It was held in *Aultman's Appeal*, 98 Pa. 505 (516), that the pledgee of stock as collateral transferred and standing in his name, is as to

* A portion of the opinion omitted.—Eds.

the corporation the legal owner, and liable for assessments, etc., just as if he was the actual beneficial owner. If he is thus charged with the burdens of ownership, it would seem to follow that he is entitled to the corresponding rights and privileges.

These being the rights of the parties under the common law, we have now to consider the effect upon them of the act of May 7, 1889, P. L. 102. (The learned justice held that the act in question did not change the rule of the common law.)

The by-laws of the corporation provide that all persons holding shares "either in their own right, or as trustees," shall have the right to vote. In this there is no restriction as to the kind of trustees or the mode or purpose of their appointment as such. It is admitted that Messrs. Watson and Wood held the title to the stock which was entered on the corporation books in their names as trustees. It is also admitted that they were pledgees, but it does not appear that the pledgors had reserved the right to vote. Both by the common law and the corporate by-laws, therefore, they were entitled to vote. It was a right of property incident to their legal title to the stock, and the declaratory and directory provisions of the statute did not take it away. Their votes should have been received and counted.

Decree *reversed*, and record remitted for further proceedings in accordance with this opinion.⁴

SMITH v. SAN FRANCISCO &c. RY. CO.

1897. 115 Cal. 584, 47 Pac. 582.⁵

APPEAL from a judgment of the Superior Court of the City and County of San Francisco and from an order denying a new trial. J. M. Seawell, Judge.

The facts are stated in the opinion of the court.

HARRISON, J.—At the election for directors of the San Francisco & North Pacific Railway Company, which was had at the annual meeting of the stockholders held February 25, 1896, the votes offered by Peter Gundecker, G. E. Wagner, and Sidney V. Smith, in

⁴ See also *Smith v. San Francisco &c. R. Co.* (1897) 115 Cal. 584, 47 Pac. 582, 35 L. R. A. 309, 56 Am. St. 119; *Miller v. Murray* (1892) 17 Colo. 408, 30 Pac. 46; *Matter of North Shore &c. Ferry Co.* (1872) 63 Barb. (N. Y.) 556 (personal representative can vote stock); *Hoppin v. Buffum* (1870) 9 R. I. 513, 11 Am. Rep. 291.

That bondholders cannot vote, see *Durkee v. People* (1895) 155 Ill. 354, 40 N. E. 626, 46 Am. St. 340.

Cumulative voting, though unauthorized at common law, is now frequently permitted. See *Chicago Macaroni Mfg. Co. v. Boggiano* (1903) 202 Ill. 312, 67 N. E. 17, reversing in part, (1902) 99 Ill. App. 509; *State v. Stockley* (1887) 45 Ohio St. 304, 13 N. E. 279; *Pierce v. Commonwealth* (1883) 104 Pa. St. 150 (constitutional right).—Eds.

⁵ Portions of the opinion and dissenting opinion omitted.—Eds.

whose names certain shares of stock stood on the books of the corporation, were rejected, and, at the close of the election, the chairman of the meeting announced that Antoine Borel, A. W. Foster, Andrew Markham, P. N. Lilienthal, George A. Newhall, James B. Stetson, and John L. Howard, had been duly elected directors of said corporation for the year then next ensuing. The votes of Dundecker and Wagner were rejected upon the ground that they were not bona fide stockholders in the corporation, and the vote of Smith was rejected upon the ground that by virtue of a certain agreement between him and two other stockholders—Foster and Markham—the stock of the three had been pooled for the term of five years, to be voted as a unit, and was cast in pursuance of that agreement. If the votes thus rejected had been received, the election would have resulted in the choice of Smith as one of the directors instead of Lilienthal. (The present action was brought under Section 315 of the Civil Code, for the purpose of having it declared that Smith instead of Lilienthal was elected a director at said election.) The superior court found that Gundecker and Wagner were bona fide stockholders, and that their vote should have been received, and that the agreement by Smith with the other stockholders did not preclude him from the right to vote the stock standing in his own name as he might choose, and that the vote by the other stockholders for his stock was unauthorized, and his own vote should have been received. Judgment was thereupon rendered that Lilienthal had not been chosen as a director, and was not entitled to exercise the office, and that at the said election Smith was chosen one of the directors, and was entitled to be so recognized. A motion for a new trial on behalf of the defendants was denied, and from both the judgment and the order denying the new trial appeals have been taken. * * *

The Smith Stock.—The exclusion of the vote tendered by Smith upon the stock standing in his name was by reason of the following facts: In February, 1893, the estate of James M. Donahue, deceased, was the owner of forty-two thousand shares or thereabouts of the capital stock of the defendant railway company, which the superior court of Marin county had ordered to be sold in the course of the administration of his estate. Prior to the sale an agreement was entered into between Smith, Foster, and Markham for the purchase of this stock as an entirety, upon the representations of Smith that upon acquiring the shares an agreement would be made by them whereby, in order to secure the control of the management and business policy of the railway company, and for its prudent and economical management in the interest of all of its stockholders, the said forty-two thousand shares should, for the term of five years thereafter, be voted as a unit in the election of directors of said railway company. In pursuance of this agreement Smith and Foster, on the 24th of February, made their joint bid for the shares, offering to purchase them as an entirety for the sum of eight hundred

action

*presenting
in court*

thousand dollars and upward, and by order of court their bid was accepted, and on March 23 the sale was completed and the price paid. After the making of the bid, and before the consummation of the purchase and completion of the sale, Smith prepared the agreement for the voting of the shares as a unit that had been contemplated by the parties to the purchase, and on the 22d of March the same was executed in triplicate between Smith, Markham, and Foster. By this instrument, after reciting therein that the parties thereto had purchased the forty-two thousand shares of stock, and had agreed to retain the power of voting the stock for five years, "so as to keep the control of the corporation from passing to persons other than themselves," it was "mutually agreed between said Foster, Markham, and Smith that they will, during said period, retain the power to vote said shares in one body, and that the vote which shall be cast by said shares, whether for directors or for any other purpose, shall be determined by ballot between them or their survivors." It was in the contemplation of the parties to the agreement that they might sell or otherwise dispose of some of the shares, and, accordingly, they made provision in this instrument for retaining the right to vote the stock so sold by them, and annexed thereto the form of an agreement to be taken by them from their vendees. This form or draft recited the purchase of the forty-two thousand shares by Foster, Smith, and Markham, and that, "for the purpose of keeping control of said road in the interest of themselves and of all persons who shall buy any portion of the stock from them," they have agreed that for the period of five years "they shall vote the said stock in one block" at all elections for officers. The purchase of the stock by Foster, Smith, and Markham was completed and the price therefor paid on the 23d of March, and twelve thousand three hundred and thirty-six shares of the stock were transferred on the books to each of them—five thousand shares being left in the name of the Mercantile Trust Company, subject to some prior trust. Prior to the day for the election in 1896, a conference was called to be held between Foster, Smith, and Markham, upon proper notice therefor, to determine by ballot how the vote of the shares should be cast at the next annual meeting for directors, and, in accordance with said notice, said conference was held, at which Foster and Markham were present, and, upon a ballot had thereat, it was determined that said shares should be voted for Markham, Newhall, and Lilienthal as directors. * * * It was shown at the trial that at the meeting of the stockholders, held on February 25th, Smith tendered a vote for the shares standing in his name, and, at the same time, Foster presented the vote of the same stock by himself and Markham in behalf of Smith. Mutual protests against the votes were made by different stockholders, and the vote cast by Foster and Markham was received and counted, and that cast by Smith was rejected. Smith also testified that, after receiving the notice for the conference to determine the bal-

agreement

lot to be cast, he informed Foster and Markham that he did not recognize the validity or legality of the agreement, and that he withdrew from the same, and would not be bound by anything which they might do thereunder. * * *

The instrument executed between the parties must, therefore, be held to be a proxy, and to authorize the vote of the forty-two thousand shares of stock to be cast in accordance with the determination of the majority of the parties thereto, and, if it was made upon a consideration sufficient to bind the parties to its enforcement, it must be regarded as still operative. One of the inducements for the purchase of the stock, and under which the parties entered into the agreement, was that the shares should be voted in one body, and held for five years as a unit. * * * The agreement between them was with reference to the forty-two thousand shares of stock, and that it should be voted as a unit, and the purpose of the agreement was the economical management of the road, and to prevent irresponsible persons from getting control. It was within the power of the parties to contract in reference to this property as fully as with regard to any other property. They were at liberty to make as a condition of their purchase that its management should be held by either of them, or by a majority of the three, and the terms of the agreement for such purchase could not be repudiated by either after the purchase had been made. It may be assumed that neither of the parties would have entered into the transaction, or agreed upon the purchase of the stock, except upon these conditions, and it must be held that each contributed his money to the purchase of the stock upon the promise made to him by the others. There was thus a sufficient consideration for the agreement granting the right to vote the stock. It was in the nature of a power coupled with an interest, and, being given for a valuable consideration, could not be revoked at the pleasure of either. (Hey v. Dolphin, 92 Hun, 230.)

Although the court in excluding this evidence, assumed that the instrument was valid, counsel for respondents have presented an argument in support of their further objection thereto, that the instrument is invalid by reason of being against public policy, and it therefore becomes necessary to consider this objection, inasmuch as the action of the court, rather than its reason for so acting, is to be reviewed; for, if the instrument is invalid, the refusal of the court to allow any effect to be gained from its exercise was proper.

"Public policy" is a term of vague and uncertain meaning, which it pertains to the law-making power to define, and courts are apt to encroach upon the domain of that branch of the government if they characterize a transaction as invalid because it is contrary to public policy, unless the transaction contravenes some positive statute or some well-established rule of law. * * * It is not in violation of any rule or principle of law for stockholders, who own a majority of the stock in a corporation, to cause its affairs to be man-

aged in such way as they may think best calculated to further the ends of the corporation, and, for this purpose, to appoint one or more proxies who shall vote in such a way as will carry out their plan. Nor is it against public policy for two or more stockholders to agree upon a course of corporate action, or upon the officers whom they will elect, and they may do this either by themselves, or through their proxies, or they may unite in the appointment of a single proxy to effect their purpose. Any plan of procedure they may agree upon implies a previous comparison of views, and there is nothing illegal in an agreement to be bound by the will of the majority as to the means by which the result shall be reached. If they are in accord as to the ultimate purpose, it is but reasonable that the will of the majority should prevail as to the mode by which it may be accomplished. It would not be an illegal agreement if articles of partnership should provide that stock in a corporation owned by the partnership, though standing in the individual names of the partners, should be voted by one of its members, and it is no more against public policy for such an agreement to be entered into between stockholders whose interests in the stock are separate than where their interests are joint. Viewed from considerations of public policy merely, it is immaterial whether such an agreement is made by the members of an existing partnership, which owns the shares, or in pursuance of an agreement by two or more persons to form a partnership for their purchase, or to purchase them for their joint account, or as one of the terms of an agreement for their purchase, by persons who contemplate no relation to each other further than that of owning stock in the same corporation. Such agreement would, in any case, be outside of the corporation and disconnected with the interest of every other stockholder, and, in either case, the same rules would control. Whether such an agreement is illegal, so that any action or vote under it can be set aside, or is of such a character that it will not be enforced, will depend upon the object with which it is made, or the acts that are done under it, and will be governed by other rules of law. * * *

The authority thus referred to is *Faulds v. Yates*, 57 Ill. 416; 11 Am. Rep. 24. In that case *Faulds* was the owner of a majority of the shares of stock in a corporation, and entered into an agreement with the defendants in the nature of a partnership for the working of a mine, and for the purchase by the defendants from him of two-thirds of his stock. It was provided in the agreement between them that they would elect the directors of the company; that they would determine among themselves as to the officers and management of the company; and that, if they could not agree, they would ballot among themselves for the directors and officers, and that the majority should rule, and their vote be cast as a unit so as to control the election. In an action for a dissolution and accounting of their partnership, it was contended that this portion of the agreement was void as against public policy and was invalid for the reason

that it was in conflict with the interests of the other stockholders. The court, however, held otherwise, using the following language: "There was nothing unlawful in it. There was nothing which necessarily affected the rights and interests of the minority. Three persons owning a majority of the stock had the unquestioned right to combine, and thus secure the board of directors and the management of the property. If one man owned a majority of the stock, he surely had the right to select the agents for its honest management." In *Hey v. Dolphin*, 92 Hun, 230, the parties were jointly interested in certain shares of stock which had been issued to them in a single certificate, and it was agreed between them that the stock should not be sold, or in any manner disposed of, or the certificates surrendered, for a period of ten years, without their joint consent in writing, but should remain as first issued, "for the purpose of enabling the said parties of the first part to prevent the control and management of the company from passing over to persons who might be less qualified or less disposed to make the business of the said company a success and its stock valuable." By the same agreement *Dolphin* was appointed a proxy to vote the whole of said shares at all elections, and the proxy was made irrevocable for ten years unless sooner revoked by joint consent. In an action brought for the purpose of having the agreement declared void, and that there be issued to the plaintiff certificates for one-half of the shares, the court held that the agreement was not void or against public policy, saying: "The object and purpose of the arrangement, as stated in the contract, is not of itself vicious, but rather the contrary. This is not a case where, as in some of the cases cited by the respondent, there is a combination of stockholders for the special benefit of some party, or where the power to cast the vote is in a party having no beneficial interest. The arrangement purported to be for the benefit of all the stockholders, and the attorney was one of the parties beneficially interested. It will hardly be claimed that a majority of stockholders may not combine to control an election of directors." (See, also, *Havemeyer v. Havemeyer*, 43 N. Y. Sup. Ct. 506; *Brown v. Pacific Mail S. S. Co.*, 5 Blatchf. 525.)

2 Cases
where public
policy.

In cases of "voting trusts," where the owners of stock transfer the shares to trustees, with authority to vote at elections according to the direction of a majority of those holding trust certificates, and the only consideration for such transfer and agreement is the mutual promises of the several stockholders, it has been held that any stockholder may revoke his agreement and withdraw his stock at will; and it is also held that stockholders, who become such after an agreement of this nature is entered into, are not bound by its terms, but will hold their shares freed from the limitations of the agreement. (*Fisher v. Bush*, 35 Hun, 641; *Woodruff v. Dubuque, etc., Co.*, 30 Fed. Rep. 91; *Brown v. Pacific Mail S. S. Co.*, 5 Blatchf. 525; *Griffith v. Jewett*, 15 Week. Law Bull. 419.) In *Moses v.*

Scott, 84 Ala. 608, certain stockholders had formed a voting trust, and placed their stock in the hands of four trustees, with power to vote the stock as a unit at all meetings, as three of them should think best, or, if they failed to agree, as three-fourths of the stock represented should determine, and had agreed not to sell their stock so pooled for three years. There was no consideration for this agreement other than the mutual promise of the several stockholders; and, while the court refused to enforce the agreement concerning the sale, upon the ground that it was in restraint of the free alienation of property, it said: "We cannot say there is anything per se illegal in an agreement entered into by and between certain stockholders in a joint stock company by which they promise to vote together as a unit in all matters pertaining to the government of the corporation. Each member has the clear right to cast his ballot as he pleases, wisely or unwisely, and no other stockholder can control his conduct or gainsay his discretion, and it can make no difference if several stockholders uniformly vote together, or so vote in obedience to a prior agreement that they will do so. The vote, when cast, is but the expressed wish of the stockholder, or at least must be so regarded, and no other stockholder can be supposed to be injured thereby. To hold otherwise would greatly abridge the voter's right to cast his ballot as he pleased."

The agreement in question cannot be regarded as illegal by reason of being in restraint of trade. * * *

Neither is it illegal or against public policy to separate the voting power of the stock from its ownership. The statute authorizes the stockholder to vote by proxy; and it was held in *People's Bank v. Superior Court*, 104 Cal. 649, 43 Am. St. Rep. 147, that a by-law restricting the selection of proxies to stockholders was invalid; that the statute places no limitation upon the right of selection, and that a stockholder may appoint as his proxy one who is an entire stranger to the corporation. The right to appear by proxy implies of itself that the voting power may be separated from the ownership of the stock, and, unless the authority of the proxy is limited by the terms of his appointment, he is necessarily required to use his own discretion in any vote that he gives. Being the agent of the stockholder, he is required to exercise this discretion in behalf of his principal; but he is at liberty to use his own discretion as to the means by which his principal's interest will be best subserved. The cases in which it has been said that the stockholder could not divest himself of the voting power of his stock, and that it should not be separated from the ownership of the stock, were cases which involved either the sufficiency of the agreement by which the voting power was transferred, or the validity of the purpose for which the power was to be exercised. The proxy must exercise a discretion of the same nature as that which the stockholder is authorized to exercise, and an authority to do otherwise would be invalid; but the authority to exercise a discretion differs from an

authority to perform a particular act. Under an appointment without words of limitation the proxy may act against the interests of the stockholder, or even against the interests of the corporation, and the corporation, as well as the stockholder, will be bound by his act as fully as if the stockholder had acted in person, while, if the authority had been directed in terms to that act, it might have been invalid. The distinction is that between an unlawful exercise of a lawful power, and the attempt to authorize the exercise of an unlawful power. The question has been presented in cases of voting trusts, but an examination of these cases will show that the question has arisen either when the authority was expressly given to carry out some illegal purpose, or when, having been given without any consideration, though purporting to be for a definite term, subsequent owners of the stock have sought to revoke it before the expiration of the term. (Shepaug Voting Trust cases, 60 Conn. 553, sometimes reported under the name of *Bostwick v. Chapman*; *White v. Thomas Inflatable Tire Co.*, 52 N. J. Eq. 178.) We have been cited to no instance where the purpose of a proxy given upon a sufficient consideration was lawful, and the person by whom the proxy was created continued to be the owner of the stock, in which the agreement has been held invalid. The stockholder cannot separate the voting power from his stock by selling his right to vote for a consideration personal to himself alone, any more than he could agree for the same consideration to cast the vote himself, and an agreement with others to appoint a proxy upon the same considerations would be equally invalid. * * * It was upon this principle that the agreements in *Hafer v. New York, etc.*, R. R. Co., 14 Week. Law Bull. 68, *Guernsey v. Cook*, 120 Mass. 501, and *Fennessy v. Ross*, 5 N. Y. Sup. Ct. App. Div. 342, were held invalid. The same principle was declared in *Gage v. Fisher*, 65 N. W. Rep. 809. In *Mobile, etc., R. R. Co. v. Nicholas*, 98 Ala. 92, the court held that there was nothing illegal or contrary to public policy in separating the voting power of the stock from its ownership, saying: "Where a proxy is duly constituted, and the power of the appointment is without limitation, the vote cast by the proxy binds the stockholder, whether exercised in behalf of his interest or not, to the same extent as if the vote had been cast by the stockholder in person. The invalidity of acts of this character by a proxy, rightly understood, is not made to rest upon the ground that there has been a separation of the voting power from the stockholders, but because of the unlawful purpose for which the proxy was appointed, or the unlawful end attempted to be effected by the exercise of the voting power." * * *

The judgment and order denying a new trial are *reversed*.

Van Fleet, J., McFarland, J., and Henshaw, J., concurred. Beatty, C. J., dissented.*

* *Faulds v. Yates* (1870) 57 Ill. 416, 11 Am. Rep. 24; *Brightman v. Bates* (1900) 175 Mass. 105, 55 N. E. 809, *Accord*. In the last cited case, Holmes, C. J. said: "We know nothing in the the policy of our law to prevent a

KREISSL v. DISTILLING CO. OF AMERICA.

1900. 61 N. J. Eq. 5, 47 Atl. 471.

THIS bill was filed by Fillipp Kreissl as a stockholder in a corporation of this state known as the Distilling Company of America.

It sets forth an agreement made June 9th, 1900, between the owners and holders of shares of capital stock in the Distilling Company of America who should subscribe and become parties thereto, therein called the "stockholders," parties of the first part; William L. Bull, William F. Harrity, Rudolph Keppler, Alvin W. Krech and Richard Sutro, therein called "the committee," parties of the second part; the Mercantile Trust Company, therein called "The Trust Company," party of the third part, and August Belmont, John L. Cadwallader, T. Jefferson Coolidge, Jr., William F. Harrity and Alvin W. Krech, therein called "the trustees," parties of the fourth part.

The agreement recites as follows:

"Whereas the parties of the second part are a committee acting at the request of holders of shares of the capital stock of the Distilling Company of America, for the purpose of instituting an inquiry into the affairs of the company, and recommending such action as might be for the benefit of the stockholders, and whereas said committee has made a report to the stockholders, bearing date June 1st, 1900, a copy of which is hereto attached and made a part hereof, and has recommended that the stockholders deposit with the trust company, subject to the order of the committee, their certificates of stock, for the purpose of transferring the same to the trustees, who for the period of five years from the 1st day of July, 1900, shall be the owners thereof under the provisions of this agreement."

The agreement also contains, among others, the following provisions:

"1st. The stockholders respectively agree that they are the owners and holders of shares of stock of the said company to the amount at par respectively set opposite their names or deposited as hereinafter provided; that they will at once deposit with the trust company, in accordance with and

~~majority of stockholders from transferring their stock to a trustee with unrestricted power to vote upon it. * * *~~ A stockholder has a right to put his shares in trust, whatever his motive. If the trust is an active one he cannot terminate it at will, and the attempt to cut himself off by contract, instead of by the imposition of duties, from ending it, certainly is not enough to poison the covenant with the plaintiff. See *Williams v. Montgomery*, 148 N. Y. 519, 525. It might be held that the duty of voting incident to the legal title made such a trust an active one in all cases." See also article, "Corporate Voting and Public Policy", in 10 Harv. Law Rev. 428.

Stockholders have no common-law right to vote by proxy. *McKee v. Home &c. Trust Co.* (1904) 122 Ia. 731, 98 N. W. 609; *Commonwealth v. Bringhurst* (1883) 103 Pa. St. 134, 49 Am. Rep. 119. See article on "Law of Business Corporations" by S. Williston in 2 Harv. Law Rev., at p. 158. The right today is ordinarily conceded by statute, although by-laws authorizing voting by proxy have been upheld in the absence of express authorization. *People v. Crossley* (1873) 69 Ill. 195.—Eds.

subject to the terms of this agreement, at its office in the city of New York, the said stock to be disposed of as herein provided, and will execute and deposit with the said trust company transfers of said stock and any powers of attorney or other documents necessary to transfer the legal title to said stock to said committee, in order to empower said committee to fully carry out the provisions and exercise the authority set forth in this agreement, and will accept in place of said stock negotiable certificates of deposit signed by the said trust company, in suitable form, to be prescribed by said committee.

"2d. The committee shall cause said stock to be transferred on the books of the company into the names of the trustees when a majority of the entire capital stock shall have been deposited, or sooner if the trustees shall request the same, and receive from the Distilling Company of America a single certificate, or certificates, in such amounts as may be convenient, in the names of the trustees in lieu thereof, such certificate or certificates to be lodged with said trust company, subject to all the terms and conditions of this agreement.

"3d. The committee is authorized and empowered to consider and present to the trustees the best means in their judgment of providing the said Distilling Company of America with such additional capital as may in the opinion of the trustees be necessary for the purposes of said company, and for the issue of such bonds, mortgages or other obligations as may be deemed advisable; provided, however, that such means so to be proposed shall not involve the assessment of any sum of money to be paid by the said stockholders. When the committee shall have presented the said subject, and the same shall be agreed on by the trustees, with such modification or changes as may be proposed thereto by the trustees, the same shall be signed by the trustees or a majority of its members and shall be filed or lodged at the office of the trust company in the city of New York, with which copies shall be left for distribution to the stockholders, and a brief publication of the fact of the adoption of the best means in their judgment referred to, shall be made at least twice in each week for at least two weeks, in two newspapers published in the city of New York, and one each in the cities of Boston, Philadelphia, Louisville, Cincinnati and Chicago; and such lodgment of such plan, and such publication thereof shall be conclusive notice to all stockholders and to all holders of certificates of deposit, of the adoption thereof; provided, however, and it is made an express condition of the execution hereof by the stockholders, that any holder of such certificates of deposit who may not agree to such plan within fifteen days after the expiration of such publication, may withdraw from this agreement and be entitled to a return of his said stock by filing with said trust company, at its office in the city of New York, written notice of his election so to do; whereupon said holder shall be released from the obligations of this agreement and from such plan, and shall be entitled to a return of his stock and receive it upon surrender of the certificates of deposit issued for the same without deduction for expenses or otherwise; but as to every certificate holder who shall not within said period make and file such notice in writing, his assent to and ratification of such plan shall be conclusively and finally assumed, conferred and given, and shall be irrevocable; and provided further, however, that the trustees shall have liberty to proceed to execute such plan and this agreement, irrespective of the parties so withdrawing, and such withdrawing parties shall have no further interest of any kind under this agreement or such plan, except upon such terms as the trustees may prescribe.

"4th. The trustees are hereby given full authority and power to carry out and put into effect the plan to be adopted by it as aforesaid, and to take any and all steps necessary to such plan, or which in its judgment may tend to promote the same, subject to the rights of the holders of the certificates of deposit to dissent therefrom and withdraw from this agreement as hereinbefore provided.

"5th. This agreement is made upon the condition that the stockholders

of said Distilling Company of America who do not sign this agreement, or do not deposit their certificates of stock in accordance with its terms, shall have no rights and be entitled to no benefits under the same, except that the committee is empowered to extend the time in its discretion, in which holders of stock may assent to and come in under this agreement or the plan to be hereafter adopted, and to admit such stockholders to participation in the benefits thereof upon such conditions and penalties as the committee and the trustees may decide.

* * * * *

"8th. This agreement and the means adopted for raising additional capital shall respectively become binding and effective whenever a majority of all outstanding stock shall assent thereto, or whenever, in the judgment of the trustees a sufficient number of stockholders have signed this agreement or deposited their stock.

* * * * *

"12th. The trustees agree that they will vote upon the shares of stock standing in their names at all meetings of the stockholders of the Distilling Company of America for such directors and for such measures as shall in their judgment be for the best interest of the stockholders."

The bill further charges that the parties are proceeding to perform and carry out this agreement, and that the trustees propose to vote upon the stock so transferred to them, at the next election, for directors of said distilling company. The bill charges that the agreement in respect to the above provisions and others, infringes upon his rights as a stockholder in said company.

To this bill the Distilling Company of America, and the persons named in the agreement as trustees were made parties defendant. Among the prayers of the bill was one for an injunction restraining the trustees from voting upon any of the stock deposited with the Mercantile Trust Company under the agreement, at any meeting of the stockholders of the company, except to adjourn the same from time to time.

* * * * *

MAGIE, Chancellor.

The complainant, as the owner of eighty-five shares of preferred stock and four hundred and twenty shares of common stock of the Distilling Company of America, each share being of the par value of \$100, seeks relief which will affect stockholders of the company owning shares of both kinds of stock amounting at par to about \$54,000,000, but of a total of stock issued amounting at par to about \$75,000,000. The holdings of complainant are therefore comparatively small; but, however insignificant his interest may be, he is entitled to relief against inequitable conduct which does or may injuriously affect his interest. The comparatively small amount of interest should, doubtless, lead the court to scrutinize his claim with care, and not to interfere with interests in the same property which are vastly greater, except it is necessary for his eventual relief upon the final hearing. * * *

Whatever deficiencies appear in making out the charges of the bill respecting the agreement in question and what has been done under it by the affidavits annexed thereto, they are supplied by the

frank admissions of the answers and the accompanying affidavits, which make clear the facts on which complainant bases his contention.

Those facts are that an agreement such as is set out in the bill was made and executed by all the parties; that the party of the first part consisted of stockholders of the Distilling Company of America who joined in the deposit of their certificates of stock in the manner prescribed therein; that stockholders holding stock to the par value of about \$54,000,000 have done so, and that the several parties intend to proceed and perform the agreement. If carried out, the trustees may vote at the coming election for directors, fixed by the by-laws of the company for October 17th, 1900, and having a large majority of the stock, their vote thereon would elect directors.

In *Taylor v. Griswold*, 2 Gr. 222, the supreme court, in dealing with the question of the reciprocal rights and duties of shareholders of private corporations, established the principle that the obligation and duty of incorporators to attend in person at meetings of the corporation and execute the trust or franchise reposed in or granted to them, is implied in, and forms part of, the fundamental constitution of every charter in which the contrary is not expressed. They thereupon denied the right of such corporation to authorize any stockholder to vote by any power of attorney or proxy, unless power to do so had been expressly or impliedly conferred by the legislature. This conclusion was reached on the avowed ground that by the association of the individuals in such corporation, each associate was expected to exercise his judgment upon all measures which he and his associates could take respecting the enterprise, which judgment his associates might assume would be favorable to his own interest and consequently beneficial to their interest. The power to judge and determine upon such measures could not, except under legislative authority, be delegated to another.

Since the decision of the case referred to, the legislature has conferred upon stockholders of private corporations, created by special laws or under general statutes, the power to appoint a proxy to cast their votes. Notwithstanding this grant of legislative authority, questions have arisen as to the extent to which stockholders may confer authority upon proxies.

The principle of that case has been applied in this court in the determination of causes involving such questions. If the present cause is essentially the same as those in which this court has already acted, I should feel it my duty to apply the same principle, even if I doubted its applicability, which I do not.

In *Cone v. Russell*, 3 Dick. Ch. Rep. 208, Vice-Chancellor Pitney held void as against public policy, an agreement between stockholders of a private corporation, by which the owners of certain shares agreed with the owners of other shares to give the latter a proxy

irrevocable for five years, and empower them to vote on the shares during that time, in consideration of which the latter parties agreed to so vote said shares as to procure the employment of one of the owners thereof as a manager of the corporation at a specified salary. This conclusion was reached notwithstanding the fact that relief by a declaration that the agreement was void was sought by one of the parties thereto, who was in *pari delicto*.

In *White v. Thomas, &c.*, 7 Dick. Ch. Rep. 178, the same vice-chancellor had to deal with a case presenting the following facts: All the holders of the stock of a private corporation which had then been issued, entered into an agreement among themselves whereby their shares were transferred to a trustee, who issued to each stockholder an assignable trust certificate for the amount of his stock so transferred. By the agreement the trustee was required to so vote upon the shares that a majority of the directors should be elected upon the nomination of holders of certain certificates, being a minority of the whole number, and a minority of the directors should be elected upon the nomination of holders of certain certificates, being a majority of the whole number of such certificates. After discussing the question whether such an agreement could be sustained as to those entering into it, for a purpose which was declared to be proper, and pointing out the apparently insuperable difficulties in carrying out its provisions, the vice-chancellor found it unnecessary to decide its validity as to the parties to the agreement, while remaining the sole owner of the stock or the beneficial interest in the stock issued; but as to the complainant who had subsequently acquired shares of stock afterwards issued, and also some of the trust certificates representing original shares, he held that the agreement was unenforceable and void as contrary to public policy.

Some expressions in these opinions have led to the contention that the vice-chancellor pronounced invalid any scheme or device by which the power to vote upon stock was separated from the ownership. That such was not his view is apparent from his language in *Cone v. Russell*, where he says: "This conclusion does not reach so far as to necessarily forbid all pooling or combining of stock where the object is to carry out a particular policy with a view to promote the best interests of all the stockholders; the propriety of the object validates the means and must affirmatively appear." It is also apparent from the later decision of the same vice-chancellor in *Chapman v. Lee*, 46 Atl. Rep. 591, where a bill was filed to set aside a power of attorney and proxy made by the complainant, conferring upon defendant very extensive powers, and irrevocable for a specified period. The vice-chancellor held that the so-called proxies were included in an instrument which clothed defendant with ownership of complainant's stock with power to sell or exchange it, or to organize a new corporation, and in that case to accept stock therein in place of complainant's shares. It was held that defendant substantially became the owner of the stock as

trustee for the complainant. Although the instrument did not set out the trust in detail, yet the court held that as such trust was set out in full in the answer, it could be taken as disclosing the purposes of the trust. Finding it established by the proofs that defendant had expended labor and money and had made contracts in reliance on the continued control of the stock, the vice-chancellor held that the agreement was not void and dismissed the bill.

Under the statutes permitting stockholders to give proxies and under the doctrine of the cases in this court to which I have referred, I conceive it is impossible to maintain that a proxy which confides to the attorney thereunder the power to exercise his judgment in certain cases, and so separates the voting power from the ownership of the stock, is void per se. The principle may, doubtless, limit the power conferred to voting on certain questions and in a certain way. But if, as is customary, the power is unlimited, it must be exercised by the judgment and determination of the attorney on any questions which may be presented.

The power of revocation is deemed sufficient to protect the rights of other stockholders. If, however, the stockholder undertakes to make irrevocable his grant of power and to denude himself for a fixed period of the power to judge and determine and vote as to the proper management and control of the affairs of the corporation, then whether the grant of power is good or not must depend on the purposes for which it is given.

When the scheme devised does not embrace a grant of irrevocable powers by proxy, but seeks a similar object by the creation of a trust and the appointment of a trustee, to whom the title of the stock is conveyed, a like doctrine must be applied. If no provision is made for the conduct of the trustee, at least he would be bound to vote on the stock held in trust in accordance with the expressed wishes of the cestui que trust; but if the transfer of the legal title to the stock is made and accepted under an agreement of the stockholders which deprives him of all power to direct the trustee, and all opportunity to exercise his own judgment in respect to the management of the affairs of the corporation, then whether the transaction is open to the objection of other stockholders, as depriving them of the right they have to the aid of their co-stockholders, must be dependent upon the purposes for which the trust was created, and the powers that were conferred.

Inde may work (If stockholders, upon consideration, determine and adjudge that a certain plan for conducting and managing the affairs of the corporation is judicious and advisable, I have no doubt that they may, by powers of attorney, or the creation of a trust, or the conveyance to a trustee of their stock, so combine or pool their stock as to provide for the carrying out of the plan so determined upon. But if stockholders combine by either mode to entrust and confide to others the formulation and execution of a plan for the management of the affairs of the corporation, and exclude themselves by acts

made and attempted to be made irrevocable for a fixed period, from the exercise of judgment thereon, or if they reserve to themselves any benefit to be derived from such a plan to the exclusion of other stockholders who do not come into the combination, then in my judgment such combination and the acts done to effectuate it, are contrary to public policy, and other stockholders have a right to the interposition of a court of equity to prevent its being put into operation.

*Duke
thar
Stinson*

The agreement in this case must be tested by these principles.

An examination of it discloses that it asserts the necessity of the corporation acquiring in some mode additional working capital. From the affidavits annexed to the answers, I think it established that notwithstanding the large assets of the company, additional capital is nevertheless deemed by the stockholders who have entered into the agreement to be judicious and necessary. To this extent the agreement indicates the judgment of those stockholders, but no plan for procuring such capital is disclosed as having been formulated or determined upon. On the contrary the formulation of such a plan is expressly entrusted to the trustees and the committee. Those stockholders, therefore, have expressed no judgment in respect to what plan should be adopted.

The respectable gentlemen who have become trustees under this agreement, detail in their answer the need of additional working capital, and the reasons why an agreement of the kind entered into might enable such capital to be procured. The motives that induced them to enter into the agreement and their present purposes in respect to its execution, are exhibited by the statements contained in the following paragraph of their answer, viz.:

"That in the early part of the year 1900 they had become more or less familiar with the affairs of the Distilling Company of America, of its financial requirements and of the needs of the constituent companies which it controlled, for additional working capital. They found that the stock of the Distilling Company of America had continuously declined in the market; that the constituent companies had ceased paying dividends and that doubt and suspicion was publicly entertained as to the ability and integrity of the management. That it was represented to them by holders of a large amount of the stock of said defendant company that no financial plan for providing the companies with additional capital could be successfully carried out unless the individuals or institutions capable of advancing such amounts of money as were required by the company for this purpose were assured of an honest and conservative management of such companies, coupled with a fixed policy for a period of years, and that such results could best be obtained through the instrumentality of a voting trust. These defendants were earnestly solicited by the holders of a very large amount of said stock to act as such voting trustees, and their services were especially solicited for the reason that none of these defendants had been previously identified with the affairs or management of the said defendant company or its constituent companies, and because they either were personally interested in the stock or represented in their individual or corporate capacity large holdings of said stock. With the exception of one of their members, none of these defendants had personal or business relations with the managing officials of the Distilling Company of America and have not met nor

conferred, either directly or indirectly, with the management of said company in reference to said voting trust; that they accepted their designation as voting trustees absolutely free from any commitment or understanding with the existing officers and directors in the belief that they could benefit the stockholders by controlling and providing capital for the purposes of the company, and by exercising a supervision over the selection of directors and officers of the defendant company and its constituent companies, and by controlling such selection could secure a conservative and fixed policy during the existence of said trust. That these defendants did not intend, and it has never been their intention, to carry out any plan for the rehabilitation of the affairs of said company which may be approved by them without first obtaining the approval of the holders of stock who have deposited their shares under the voting trust agreement;"

but they proceed further to say,

"that although no actual plan for such purpose has yet been formally settled by the committee or these trustees, various plans have been considered and are in contemplation, dependent upon the result of the examination of the affairs of the companies."

No restriction
(It is obvious, however, that these statements in nowise limit or restrict the trustees in the exercise of such powers as have been conferred, or attempted to be conferred, by the agreement in question.

But it is argued that the agreement is only tentative and the stockholders who joined therein have reserved to themselves the power, after the plan contemplated should be formulated and promulgated in the manner provided, to withdraw from the combination and receive back their stock. Such a provision is elaborately set out in the third article of the agreement. If this provision would have the effect of preventing the execution of the plan, this argument might perhaps be effective. But the proviso to that article renders the withdrawal of stock, even of all the combining stockholders, ineffective in preventing the execution of a plan devised by the trustees, because it expressly provides that the trustees shall have liberty to execute such plan irrespective of the parties so withdrawing.

It is further argued, however, that assuming that the trustees might thus proceed to execute their plan, its execution would require the co-operation of the directors of the company. I can conceive no plan which would not require the directors' action. But in considering this argument, it must be remembered that the trustees by this agreement are empowered to vote upon the stock while remaining in their names, and the amount of stock controlled by them will undoubtedly secure the election of directors. It should also be remembered that a large majority of directors are to be elected at the approaching election. It will, therefore, be seen that if the trustees vote as required under this agreement, they will elect a controlling majority of the board of directors. While I should entertain no doubt that the gentlemen composing these trustees would not take advantage of withdrawing stockholders, and

execute a plan they disapprove of, the fact that they are given express power to do so, and the power to elect the board of directors to co-operate with them, deprives the transaction of any tentative character and justifies its being pronounced contrary to public policy, in that it provides for a possible management of the affairs of the company during a fixed period of time, by the judgment and determination of others, and not by the judgment and determination of complainant's associates in this corporation.

By the provisions of the fifth article of the agreement, stockholders who do not enter into it are expressly declared to be entitled to no benefits under it. Upon the argument, the meaning of that provision was not made clear. But it is evident that the parties to the agreement conceived that assenting stockholders had an interest in carrying out this agreement which would not enure to the benefit of those who did not join in it. By the last clause of the proviso to article three this idea clearly appears. Whether the privilege of subscribing additional shares of stock issued, or taking bonds or obligations issued to raise additional capital was the benefit intended to be conferred on the assenting stockholders to the exclusion of the non-assenting stockholders, I can only conjecture. It is sufficient to say that the agreement discloses an intent to exclude stockholders who do not enter into it from whatever benefits could be claimed thereunder. [This, in my judgment, shows a combination contrary to public policy and one to which any non-assenting stockholder may object.]

There are other criticisms upon this agreement which need not now be discussed. Upon the two points above named, it is open to objection and I think the preliminary injunction should issue restraining the trustees from voting on any stock acquired by the agreement, according to the terms of the prayer of the bill.⁷

Section 2.—By-Laws.

NORTH MILWAUKEE TOWN SITE CO. v. BISHOP.

1899. 103 Wis. 492, 79 N. W. 785.

APPEAL from a judgment of the superior court of Milwaukee county: Geo. E. Sutherland, Judge. Affirmed.

The plaintiff is a corporation. The defendant is the owner of fifty-eight shares of its capital stock, of the par value of \$100, upon which assessments to the amount of \$54 have been paid. On April

⁷ See Chapman v. Bates (1900) 61 N. J. Eq. 658, 47 Atl. 638, 88 Am. St. 459; Warren v. Pim (1903) 65 N. J. Eq. 36, 55 Atl. 66, and comment on the principal case and these cases in 1 Columbia Law Rev. 56, 3 Columbia Law Rev. 482.

In Harvey v. Linville Improvement Co. (1896) 118 N. Car. 693, 24 S. E. 489, 32 L. R. A. 265, 54 Am. St. 749, Clark, J. said: "In short, all

20, 1896, the plaintiff's board of directors adopted the following resolution:

"Resolved, That a call be, and hereby is, made upon the unpaid portion of subscription for stock in this company, amounting to \$46 per share, the same to be paid thirty days from date, either in cash or by a promise to pay in the form of a land contract or contracts; and when the same shall be paid that the stock shall be shown as full-paid on the books of the company; and the secretary is hereby directed to proceed and use all legal means necessary for the collection of any unpaid portion of said call, and, if any party refuse or neglect to make such payment, proper steps be taken to advertise and foreclose the stock upon which such payment shall not have been made."

At the same time the board passed the following resolution: "Resolved, That the secretary be, and hereby is, instructed to notify the stockholders of this company of said call by mailing to each stockholder a copy of said resolution."

The defendant failed to pay the call so made, and this action was commenced to enforce payment. After hearing the plaintiff's evidence, the court granted a nonsuit. From a judgment for defendant, the plaintiff appeals.

BARDEEN, J. The judgment of nonsuit was justified upon either of two grounds:¹

2. No proof was made of giving notice of such call according to the by-laws of the corporation. Sec. 1754, Stats. 1898, provides that, "unless otherwise expressly provided by law or the articles of organization, the directors of any corporation may call in the subscriptions to the capital stock by instalments, in such proportion and at such times as they shall think proper, by giving such notice thereof as the by-laws shall prescribe."

It was admitted on the trial that no by-law of the corporation in this regard had ever been adopted. The action of the board was attempted to be justified, however, by showing that the board, after adopting the resolution for the call, adopted another resolution instructing the secretary to notify each stockholder thereof by mailing to him a copy of said resolution. This latter action of the board is claimed to be equivalent to a regular by-law, and answers all the purposes of the statute. The difficulty with this contention is that the board of directors have no power to enact by-laws unless so authorized by law, by the articles of organization, or by proper action of the stockholders. A by-law is a permanent and continuing rule for the government of the corporation and its officers. The power to enact them resides primarily with the stockholders. They

agreements and devices by which stockholders surrender their voting powers are invalid. 5 Thompson Corporations, Sec. 6604. The power to vote is inherently annexed to and inseparable from the real ownership of each share, and can only be delegated by proxy with power of revocation." So also. Shepaug Voting Trust Cases (1890) 60 Conn. 553.—Eds.

¹ Opinion given on second point only.—Eds.

have few functions to perform, and this right to make by-laws is an essential and an important one. It is a power that the directors have no inherent right to exercise. This is the rule laid down by the textwriters, and finds ample support in the authorities cited in the following works: 2 Cook, Stock, § 700a; 1 Thomp. Corp. § 956; Ang. Corp. § 327. In the Germania Case cited, it is said: "We hold, therefore, that it was intended that the statutory method of making calls should supersede previous common-law methods, and to prescribe a uniform and reasonable rule easily complied with;" and it was accordingly held that a complaint which did not allege that a call was made by giving such notice as the by-laws prescribed fails to state a cause of action. For the same reason such an action cannot be sustained until *proof* is made in conformity to these requirements. It is argued, however, that because sec. 1776, R. S. 1878, provides that "the stock, property, affairs and business" of every corporation shall be under the care of and be managed by a board of directors, the power to enact proper by-laws may be implied therefrom. As before intimated, the power to make by-laws is incident to the corporation itself, and results from the necessity of such a power to enable the body politic to answer to the purposes for which it was created. It being a valuable and important right, it ought not to be taken away by inference or implication. The power given to the directors to control the stock and business of the corporation may exist, and be entirely consistent with the power of the stockholders to say upon what terms and conditions the stock of the corporation shall be paid for and issued. We therefore hold that, unless taken away by the charter or some law of the state, the power to enact suitable by-laws rests in the stockholders of the corporation, and not in the board of directors. Our attention has been called to some expressions used in the opinion in *In re Klaus*, 67 Wis. 401, to the effect that the directors and not the stockholders, may make the by-laws. As we have seen, this statement of the law is contrary to all of the adjudicated cases, and cannot be sustained on principle, and was in fact not necessary to the question decided. In that regard it must be deemed to be overruled.

By the Court.—The judgment of the superior court of Milwaukee county is affirmed.*

FLINT v. PIERCE.

1868. 99 Mass. 68.

CONTRACT against a stockholder of the Reading Agricultural and Mechanic Association for the amount of a balance due on a prom- A

* But see *Manufacturers' Exhibition Bldg. Co. v. Landay* (1905) 219 Ill. 168, 76 N. E. 146, (power to adopt by-laws vested by statute exclusively in the directors).—Eds.

issory note of the association made by its treasurer. The declaration alleged the individual liability of the defendant on the note by reason of his subscription of the following by-law of the association: "Article 10. The members of this association pledge themselves in their individual as well as their collective capacity to be responsible for all moneys loaned to this association and for the payment of which the treasurer may have given his obligation agreeably to the direction of the defendants."

At the trial, before Gray, J., without a jury, these facts appeared: The association was incorporated by the St. of 1830, c. 41, "for the purpose of encouraging agriculture and the mechanic arts by granting premiums or loans of money, and for relieving the distresses of unfortunate mechanics and their families, and to have all the privileges usually given by acts of incorporation to charitable societies;" and was organized March 30, 1831, when it adopted by-laws, one of which was that above quoted, and another provided that "any person may become a member of this association by subscribing his name to these by-laws and paying to the treasurer the amount of one or more shares." The preamble of the by-laws was as follows: "The design of this institution is to afford to those who are desirous of saving their money the means of employing it to advantage; it is intended to encourage the industrious and prudent, and to induce those who have not hitherto been so to lessen their unnecessary expenses, and to save and lay by something for a period of life when they will be less able to earn a support."

The association never granted premiums for encouraging agriculture and the mechanic arts, nor ever made gifts for relieving the distresses of unfortunate mechanics and their families; but its sole business was the borrowing of money and discounting of notes therewith. From 1847 to 1860 it paid annual dividends of five dollars per share; and from and after 1852 its capital stock consisted of fifty shares of one hundred dollars each. The defendant subscribed his name to the by-laws, and became a shareholder and member of the association, prior to 1847. In 1859 the plaintiff lent to the association twenty-six hundred dollars, and held its notes therefor at five per cent. interest. Prior to August 29, 1862, the directors instructed the treasurer to "pay all outstanding notes which were at five per cent. interest, unless the creditors would renew them at four per cent. interest, and to renew all such as would renew at four per cent.;" and the treasurer gave notice of this direction to the plaintiff, who on that day surrendered the notes he held at five per cent., and took instead the following note for the balance due him: "Reading, August 29, 1862. The Reading Agricultural and Mechanic Association for value received promise to pay Samuel Flint or order twenty-six hundred and ninety-nine dollars in twenty days after demand, with interest at four per cent. if not paid within one year from date. Jonathan Frost, Treasurer." Upon this note the association made one payment of ninety-

nine dollars in October, 1862, and another of six hundred dollars and one year's interest in January, 1864, and then, notwithstanding repeated demands by the plaintiff, failed ever to pay the balance. More than twenty days after the last such demand the plaintiff gave the defendant notice of the failure of the association to pay the note, and demanded payment thereof from him as a member of the association, and upon his refusal brought this action.

* * * * *

WELLS, J. The note upon which this action is based is the contract of the corporation. The defendant is not a party to that contract; and the plaintiff does not seek, by this suit, to charge him upon any statute liability as a stockholder. Responsibility for the amount of the note is sought to be established through a by-law of the corporation, to which the defendant had attached his signature. This by-law, with others, was adopted in 1831. To become a member of the association it was requisite to subscribe the by-laws. It does not appear that the defendant's signature was attached for any other purpose than to constitute him a member of the corporation. It does not appear, and is not alleged, that the plaintiff lent his money upon the faith or credit of the individual pledge contained in the by-law; nor that the by-law was in any manner made known to him, or to the public, as the basis of such credit.

The office of a by-law is to regulate the conduct and define the duties of the members towards the corporation and between themselves. So far as its provisions are in the nature of a contract, the parties thereto are the members of the association, as between themselves; or the corporation upon the one side, and its individual members upon the other. The right of any third party, stranger to the association, to establish a legal claim through such a by-law, must depend upon the general principles applicable to express contracts, as laid down in Mellen v. Whipple, 1 Gray, 317, and the subsequent decisions in Field v. Crawford, 6 Gray, 116, and Dow v. Clark, 7 Gray, 198. No action can be maintained by such third party unless he can bring his case within some of the recognized exceptions to that general rule. A pledge like the one in question, if made for the purpose of enabling the corporation to obtain a loan upon the faith of it, and used for that purpose, may perhaps give a right of action against the subscribers in favor of a party who has been induced to advance money upon its credit. This seems to be implied strongly by the decision in the case of Trustees of Free Schools in Andover v. Flint, 13 Met. 543, inasmuch as the plaintiff in that case appears to have failed to recover upon a similar claim merely for the reason that the defendant had not signed the by-law. But no such facts are shown to exist in the present case. The plaintiff not only is no party to the contract contained in the by-law, but he fails to show any privity between himself and the defendant in rela-

tion to the subject matter, or to the consideration, of his demand. Judgment must be rendered accordingly for the defendant.*

IRELAND v. GLOBE MILLING & REDUCTION COMPANY.

1895. 19 R. I. 180, 32 Atl. 921.

1898. 21 R. I. 9, 41 Atl. 258.*

ASSUMPSIT for refusing to transfer stock. On demurrers to the pleas and replications.

September 19, 1895. TILLINGHAST, J. The pleadings in this case present two questions for our decision, namely, first, is the stock of a non-resident, in a foreign corporation doing business in this State, attachable here; and, second, are the by-laws of the defendant corporation set up in its third special plea in bar, taken in connection with the statutes of the State of Maine relating to the transfer of stock in corporations, which are also pleaded, effectual to prevent William R. Stearns, the assignor of the stock in question, from transferring the same to the plaintiff by a mere indorsement and delivery thereof, so as to confer upon him the right to maintain this action. * * * The third plea sets up that the defendant corporation was organized August 10, 1892, under the laws of the State of Maine, at Saco, by articles of agreement or association, to which articles said Stearns was a subscribing party, and that in the proceedings of organization he participated and was then and there elected president and a director of said corporation, which offices he filled during the ensuing year; and that then and there, as a part of the proceedings of the organization of said company, certain by-laws were unanimously adopted by said Stearns and

* In *State v. Overton* (1854) 24 N. J. L. 435, 61 Am. Dec. 671, Green, C. J. said at p. 440: "The validity of the by-law of a corporation is purely a question of law. Whether the by-law be in conflict with the law or with the charter of the company, or be in a legal sense unreasonable, and therefore unlawful, is a question for the court and not for the jury. *Commonwealth v. Worcester*, 3 Pickering, 462; *Paxson v. Sweet*, 1 Green, 196; *Ang. & Ames on Corps.* 357. But the by-laws of a private corporation bind the members only by virtue of their assent, and do not affect third persons. All regulations of a company affecting its business which do not operate upon third persons, nor in any way affect their rights, are properly denominated by-laws of the company, and may come within the operation of the principle."

See also *Smith v. Smith* (1872) 62 Ill. 493 ("Strangers to the company cannot be bound by the rules adopted for the government of the company"); *Barnes v. Black & Co. Coal Co.* (1898) 101 Tenn. 354, 47 S. W. 498.—Eds.

* Portions of opinions omitted.—Eds.

the other incorporators of the company in relation to the transfer of stock and other matters, among which by-laws were the following:

"ARTICLE III.—CAPITAL STOCK."

"SECTION 2. No stockholder shall assign and transfer his stock, or any part thereof, to any person, unless he shall first offer the same to the corporation at the lowest price at which he is willing to sell and assign the same. If in thirty days after such offer shall have been made in writing to the corporation, said corporation shall refuse or neglect to purchase the stock so offered, the owner thereof may sell and transfer the same to any other person at not less than the price stated in said offer.

"SECTION 3. Shares may be transferred by endorsement on the certificates of stock and delivery thereof, but shall not be valid (except between the parties thereto) until the same shall be recorded in proper form upon the books of the corporation. Upon surrender a new certificate or certificates shall be issued and the surrendered certificate or certificates shall be canceled and replaced and secured in the certificate book."

Said third plea then proceeds to state that said by-laws had been adopted and were in force at the time, and before the time when the certificates of stock mentioned and described in the declaration, or any certificate of stock in the said corporation, had been issued, and that all said certificates were and are subject to said by-laws and the provisions thereof, which by-laws, from their adoption till now, have been continuously in force, of which by-laws and the operation thereof said Stearns and said plaintiff, at and before the sale set out in plaintiff's declaration had knowledge; that said Stearns had not before the alleged sale offered to said corporation his said stock at any price whatever, nor had in any manner complied with the by-laws concerning the transfer of his said stock, of which non-compliance with said by-laws by said Stearns the plaintiff had knowledge at the time of and before said sale; wherefore the defendant, having said lien of option upon said stock by reason of said by-law, declined to register said transfer of said stock, because said Stearns had as aforesaid failed to comply with said by-law relating to said transfers. * * *

As to the second question. We do not think the defendant corporation had power to enact the by-law first above quoted. Section 6 of Chapter 46 of the Statutes of Maine, set up in the defendant's third special plea, provides that "Corporations may determine by their by-laws the manner of calling and conducting meetings; the number of members that constitute a quorum; the number of votes to be given by the shareholders; the tenure of office of the several officers; the mode of voting by proxy, and of selling shares for neglect to pay assessments; and may enforce such by-laws by penalties not exceeding twenty dollars." And the rule is that where by the provi-

sions of the particular charter, or by a general statute relating to corporations, power is conferred upon a corporation to enact by-laws for certain specified purposes, its power of legislation is limited to the cases and objects enumerated, all others being excluded by implication. "*Expressio unius est exclusio alterius.*" See Angell & Ames on Corporations, 5th ed. Sec. 325; *Child v. Hudson's Bay Company*, 2 P. Wms. 207; *Kennebec & Portland R. R. Co. v. Kendall*, 31 Me. 470; *Chouteau Spring Co. v. Harris*, 20 Mo. 382. The defendant corporation, then having no power to enact the by-law in question, it becomes unnecessary to consider whether or not it was a reasonable enactment, as contended by defendant's counsel.

STINESS, J.—(21 R. I. 9.) This case has been twice before the court on questions of pleading successively raised. The plaintiff sues the defendant for damages for a refusal to transfer stock upon its books to him, which had been sold to him by Wm. R. Stearns, the owner of record, by a delivery of the certificate and a power of attorney to W. H. Sweetland to make the transfer. Recalling only the pleas which relate to the question now before us, the defendant's third plea, at the first hearing, sets up the fact that upon its organization, August 10, 1892, certain by-laws were adopted, providing that no stockholder should sell his stock until thirty days after an offer to the corporation, and that shares could be transferred by endorsement on the certificates, but the transfer should not be valid, except between the parties, until the same should be recorded on the books of the company, and the plea alleged non-compliance with those by-laws.

The plaintiff in reply set up certain statutes of Maine, where this corporation was created and is located, relating to corporations, and, following the decision of the Supreme Court of Maine in *Kennebec v. Kendall*, 31 Me. 470, we held that the corporation had no power to pass such a by-law, because the statute relating to by-laws gave no authority to pass a by-law of that kind, 19 R. I. 180. The defendant then filed additional pleas, setting up the substance of the by-law as an agreement between the subscribers to the stock and the corporation. It appeared, however, that the certificate of organization was not filed with the secretary of state until August 31, 1892, and hence, by the terms of the statute, the organization did not become a corporation or become authorized to do business until that time. The corporation, therefore, could not have made such an agreement on August 10, 1892. 20 R. I. 190.

The defendant, by further amendment to the third plea, now sets up Rev. Statutes of Maine, cap. 46, Secs. 1, 2, 6, and 12, and cap. 48, Secs. 1 and 16 to 19 inclusive, under which, especially cap. 46, Sec. 2, providing that corporations may make by-laws consistent with the laws of the State, it is argued that the by-laws in question are consistent with the laws of the State and so the corporation had power to pass them, although they are not among the classes enumerated in cap. 46, Sec. 6. It is also set out that the by-laws have been continuously in force.

The plaintiff demurs to the plea as amended.

The question thus raised is the validity of the limitation of a stockholder's right to transfer his stock without first offering it to the corporation for a period of thirty days.

We fully agree with the claim of the defendant that this question should be decided according to the law of the State of Maine, and such was our effort in the previous opinion. It is a delicate, and not always a satisfactory, task to declare the law of another State. It is to be regretted that this precise question has not been passed upon by the Supreme Court of Maine, but it seems to us to be included in the ratio decidendi of *Kennebec v. Kendall*, supra. That case has been affirmed in *Jay Bridge v. Woodman*, 31 Me. 573; and in *Belfast v. Moore*, 60 Me. 561. We are not aware that it has in any way since been criticised or disapproved.

That was an action of assumpsit for a subscription to corporate stock. A by-law of the company provided that "if the shares of any such delinquent stockholder shall not sell for a sum sufficient to pay his assessments with interest and charges of sale, he shall be held liable to the corporation for any deficiency." The gist of the decision is that, although a personal obligation may be imposed upon a holder of stock by charter or statute and also by his express agreement, such obligation cannot be imposed by a by-law under the general act respecting corporations. In other words, a statutory provision that "corporations may make by-laws consistent with the laws of the state and their charters" (Rev. Stats. Me. cap. 46, Sec. 2); or that "corporations may determine by their by-laws the manner of calling and conducting meetings; the number of members that constitute a quorum; the number of votes to be given by stockholders; the tenure of the several officers; the mode of voting by proxy and of selling shares for neglect to pay assessments; and may enforce such by-laws by penalties not exceeding twenty dollars" (Rev. Stats. Me. cap. 46, Sec. 6); does not authorize a by-law which seeks to impose a personal obligation not specified in the statute and not otherwise authorized by law. The proper office of by-laws is to regulate the transaction of the incidental business of a corporation. They should not affect rights of property or create obligations unknown to the law. A majority have no right, under the form of a by-law, to impose restrictions upon a minority in the free transfer of their stock which are not specially authorized by statute or charter, or which are not reasonably necessary to the business of the corporation.

This we understand to be the doctrine of the decision in Maine. It is not based upon the fact, as assumed in argument, that no by-laws can be passed except those specially mentioned in the statute, but upon the lack of power in a corporation to restrict private rights, except in cases pertaining to the orderly conduct of affairs, of which the classes specified in the statute are examples. This is clearly brought out in *Kennebec v. Kendall*, where the court says: "The general act respecting corporations contained in the Revised Statutes,

c. 76, Sec. 6" (similar to the present Rev. Stats. c. 46, sec. 6), "authorizes them to determine by their by-laws the mode of selling shares for non-payment of assessments, but it imposes no personal obligation to pay." The charter cannot be considered as specially delegating the power to impose such an obligation not imposed by the charter or any statute provision."

It is argued that as Stearns, the assignor of the stock in this case, knew of the by-law, took part in its adoption and so assented to it, he was bound by it and could give to his assignee no greater rights than he himself had in the stock. But where the by-law was without authority of statute, it was held in *Jay Bridge v. Woodman*, supra, that it could only have the effect of a contract by, and enforceable against, the assignor, and that the assignee was not bound by it, by virtue of the assignment alone.)

(The learned judge proceeded to consider the authorities relied upon by defendant.)

These cases are cited to show that by-laws may be passed on the subjects which are not specially mentioned in the statute. We do not question this proposition, so far as they relate to the regulation of the affairs of the corporation. What we say is that, when they go beyond this and restrict the private right of a stockholder to dispose of his stock, we understand the law of the State of Maine to be that such by-laws are not authorized by the statutes of Maine. * * *

*Demurrer sustained.**

Section 3.—Dividends.

LOCKHART v. VAN ALSTYNE.

1875. 31 Mich. 76

ERROR to Superior Court of Detroit.

COOLEY, J.—The plaintiff seeks to recover of the defendant a sum alleged to be owing to the plaintiff by the Wyandotte Agricultural Works, and for which it is claimed the defendant is liable in consequence of the failure of the officers of that corporation, of whom he

* See *People's Home Savings Bank v. Sadler* (1905) 1 Cal. App. 189, 81 Pac. 1029 (commenting on principal case).

In *Driscoll v. West & C. Mfg. Co.* (1874) 59 N. Y. 96, held that a corporation cannot create or declare a lien upon its stock by by-law. Folger, J. said (p. 102): "It is not a reasonable by-law, which, without authority express or to be clearly implied, interferes with the common rights of property and the dealings of third persons, and prevents the purchase and transfer or delivery of property." *Contra*, *Grafflin Co. v. Woodside* (1897) 87 Md. 146, 39 Atl. 413; *Bronson Elec. Co. v. Rheubottom* (1900) 122 Mich. 608, 81 N. W. 563 ("According to the weight of authority, a by-law creating a lien on the shares of a member for debts due by him to the corporation is valid and binding, though not as against innocent purchasers for value").

In *Bridges v. National Bank* (1906) 185 N. Y. 146, 77 N. E. 1005, following

was one, to make and file the official reports required by law. A recovery is resisted on several grounds, but as the question of corporate indebtedness seems first in point of order, we shall consider it first.

The supposed liability arises upon a certificate of stock issued by the officers of the corporation in accordance with a vote of the board of directors, of which the following is a copy :

"Resolved, that the company issue thirty-six thousand dollars of preferred capital stock, upon which a semi-annual dividend of five per cent., payable upon the first days of March and September in each year, shall be guaranteed by the company; the first semi-annual dividend payable on the first day of September, 1872. And the holders of any such preferred stock shall have the privilege, for one year after the first day of March, 1872, of exchanging the same, if they desire, for the common stock of the company."

The certificates of stock issued under this resolution were in all respects in the usual form, but the following endorsement was made upon them: "Full paid stock; 5 per cent semi-annual dividend guaranteed from Sept. 1, 1872, Elisha Mix, Sec'y and Treas'r." The plaintiff became the purchaser of certificates representing \$2,000 of stock, upon which the company paid two semi-annual dividends, but has failed to pay any more; and it is conceded that those which were paid were not and could not be paid from profits, because there have been no profits since the certificates were issued; and the corporation has now ceased to carry on the business for which it was organized.

The statute which the plaintiff relies upon is Sec. 1821 of Comp. L. of 1857, which, on the neglect or refusal of the directors of manufacturing companies to comply with certain provisions of law regarding the filing of their articles of association, and of annual reports showing their financial condition, declares that such directors "shall be jointly and severally liable in an action founded on this statute, for all the debts of such corporation contracted during the period of such neglect or refusal." This statute, it will be perceived, only makes the directors personally liable for "debts." Liabilities of a company which may give causes of action against it and result in judgments are not within the statute unless they constitute present debts. A debt is that which one person is bound to pay to another, either presently or at some future period; something which may be the subject of a suit as a debt, and not something to which the party may be entitled as damages in consequence of a failure to perform a duty or keep an engagement. A right to a dividend from the prof-

Third Nat. Bank v. Buffalo German Ins. Co. (1903) 193 U. S. 581, 24 Sup. Ct. 524, 48 L. ed. 801, *held* that neither a provision in the articles of association or by-laws of a national bank can create such a lien. *Cf. also Mohawk Nat. Bank v. Schenectady Bank* (1894) 78 Hun (N. Y.) 90, 28 N. Y. S. 1100, (affd. 151 N. Y. 665, 46 N. E. 1149) and *Gibbs v. Long Island Bank* (1894) 83 Hun (N. Y.) 92, 31 N. Y. S. 406, 63 N. Y. St. 854, (affd. 151 N. Y. 657, 46 N. E. 1147).

See also *Nicholson v. Franklin Brewing Co.* (1910) 82 Ohio St. 94, 91 N. E. 991.—Eds.

its of a corporation is no debt until the dividend is declared. Until that time the dividend is only something that may possibly come into existence, but the obligation on the part of the corporation to declare it, cannot be treated as the dividend itself. — In *re London India Rubber Co.*, Law Rep., 5 Eq. Cases, 525-6. This seems to be conceded by counsel for the plaintiff, who insist that the guaranty in this case is not of dividends to be made necessarily of profits, but of dividends to be made from some sum which the corporation undertakes to set apart for the purpose, and which, if there are no profits for the purpose, there is an absolute and unqualified obligation to pay from some other source. In other words, that the word "dividend" means only something to be divided; and to the persons who are to participate in the division it is immaterial whence it comes, so that the fund be actually provided, and payment made in pursuance of the obligation.

We are referred to no authority in which the word dividend has been interpreted in accordance with this view, nor are we aware that it is used in this sense among business men. A dividend to the stockholders of a corporation, when spoken of in reference to an existing organization engaged in the transaction of business, and not of one being closed up and dissolved, is always, so far as we are aware, understood as a fund which the corporation sets apart from its profits, to be divided among its members. A corporation of which it is said that it is making an annual dividend of ten per centum upon its stock, is supposed to be a prosperous corporation, because its gains leave it this clear annual per centage, which it can pay over without impairing its capital. A dividend among preference stockholders exclusively, is understood to imply that the sum divided has been realized as profits, though the earnings do not yield a dividend to the stockholders in general. We hazard nothing in saying that this is the primary and universal understanding of a dividend on stock, except when made use of in respect to a final closing up and distribution of assets on the occurrence of insolvency or in view of a dissolution. This is manifestly the view of the court in *Stevens v. South Devon Railway Co.*, 9 Hare, 312; *Henry v. Great Northern Railway Co.*, 1 De Gex & Jones, 605; *Taft v. Hartford P. & F. Railroad Co.*, 8 R. I. 310; and in every other case in which we have found the word employed in any connection corresponding to that in which it is made use of here.

The difficulty in this case springs from the fact that in the case of this corporation there are no profits from which a dividend can be made. The question arises, in view of that fact, whether the guaranty becomes wholly inoperative for want of something to which it is applicable, or whether on the other hand, it can be understood as binding the corporation to make payment of the dividend in any contingency, and to respond in damages to an equivalent amount in case of failure. The latter is the theory of the present suit; the plaintiff reading the guaranty as a promise in perpetuity to pay a semi-annual

dividend of five per centum to the preference stockholders, profits or no profits; in other words, to pay it from profits if any there are, but if not, then from whatever assets or means the corporation may possess, so long as anything shall remain to pay with.

If this be the correct view to take of the guaranty, it involves some results which will certainly be extraordinary. Whatever shall be the construction of this instrument, it will still remain true that a dividend, as generally understood, and as the public will understand it, is a sum which can be divided among stockholders without touching the capital stock. The declaration of a dividend is a most emphatic assertion that the corporation is in condition to make a division of profits, and is consequently enjoying some degree of prosperity. So generally is this understood that the making of a dividend when the capital must be encroached upon for the purpose, is looked upon as highly discreditable, if not absolutely dishonest and fraudulent, as involving an assertion of prosperity which, under such circumstances, would be deceptive, and tending to give to the corporation a credit to which it is not entitled. The corporation which should make such a dividend would, when the facts became known, be condemned by the public sentiment, and the officers who should participate, would be looked upon as wanting in that business integrity which is essential to entitle them to public confidence. So forcibly has this been felt, that the legislature in providing for the formation of corporations has, in some cases, imposed penalties upon the corporate officers who participate in making dividends when the corporation is not in condition to warrant it; and this legislation is only an expression of the public sentiment, which condemns such action as unwise and misleading, and every way impolitic. And the impolicy is only emphasized and made the more distinct and manifest by the circumstances which surround this case.

For here the preference stock upon which the dividends were to be paid was issued for the purpose of strengthening the corporation, and giving it the necessary means to put itself on a footing of success. Indeed, the issue of such stock can very seldom be justified, except to strengthen the corporate standing, or to enlarge the corporate means and business. The issue is usually made when the corporation has reached a crisis in its affairs, and the corporators are unable or unwilling to put more means at risk in the business, but are nevertheless disposed to give to those who will do so, a first participation in any profits which the increased means will enable them to make. The contracts made under such circumstances, usually in express terms confine the advantages of the new stockholders to this preference; and thus confined, there can be no reasonable objection to them, if they are entered into with full knowledge on the part of all concerned. But the guaranty in this case is understood to go farther, and not only give a preference in the division of profits, but to entitle the holder to such an apportionment of the assets of the corporation from year to year, when there are no profits, as may eventu-

ally consume the whole, leaving the other stockholders nothing. It is not a mere preference that is given to the holders under this construction; it is a preference with a perpetual promise to pay the largest interest permitted by law on the sum invested by them, profits or no profits; so that the holders have at the same time all the advantages of stockholders and of creditors, while their associates are postponed as stockholders, and, considered as representing the debtor corporation, they are deprived by the very contract itself of any reasonable probability of restoring the standing and strength of the corporation when once it shall have ceased to be steadily and continuously prosperous. For an agreement to pay semi-annual dividends from earnings when there are any, and from capital when there are not, is only a new form of the undertaking by which the debtor is to pay from his profits if the ship comes in, and from the pound of flesh if it does not; every dividend from the capital being an attack upon the very life of the corporation, before which, under ordinary circumstances, it must inevitably and speedily give way. And thus the contract, the only justification for which is the strengthening of the corporation, is found to contain within itself a provision which, except in the event of steady prosperity, must inevitably tend to its weakening, and almost certainly to its destruction.

It may be well also to consider what would be the position of the two classes of stockholders,—the common and the preferred,—with reference to the corporate management and business. Both, without doubt, have an equal right to participate in management, and officers may be chosen indifferently from either. Either class may be the larger, and by a combination of its members may secure control. Now, the earning of a dividend in any business depends more or less on many external circumstances,—on the general state of trade in the country, competition in the particular business, the condition of crops, accidents of fire and flood, new inventions affecting the use or the profitableness of machinery employed or fabrics produced, the dishonesty or carelessness of subordinates, and a thousand other circumstances which may seriously affect earnings, but against which care and foresight can but imperfectly provide. But perhaps more than on all these circumstances, a dividend will depend on the good judgment, fidelity and integrity of the managing parties; and the officers of a corporation who agree on its behalf to earn and pay one, can only be understood as undertaking for whatever good judgment, integrity and fidelity can accomplish. In this view the contract in question can only be regarded, on the plaintiff's own construction, as a contract of guaranty that the integrity and good management of the officers shall produce the dividends. But suppose those officers to be,—as they well may be,—preference stockholders themselves; then we have the corporation guaranteeing to them their own integrity and good management, and promising to make up to them from its capital whatever in expected results that management may fail to realize.

But these are not the only anomalous results that may flow from such a construction. To the success of a corporation it is important, if not essential, that there should be substantial harmony of interests among the corporators. Such harmony may exist among common and preference stockholders if the preference extends only to a division of profits, but when it goes farther, it disappears, and antagonism necessarily comes in. A preferred stockholder who is entitled to his dividend in perpetuity is interested in keeping a failing concern in existence until his dividends can wholly exhaust its means. A common stockholder is interested in bringing about a dissolution, because when that takes place, the dividends will cease, the assets must be divided, and he may have a share. The whole capital and assets of the concern may consequently be at issue between these classes in the corporate elections; the one class anxious to put an end to the corporation, because only in that event can they have anything to withdraw, while the other are concerned if possible to keep its means locked up where they are, though they may have wholly ceased to accomplish the ends of the corporate existence, because in that way they may at length absorb the whole. It may safely be asserted that legislation would never purposely have placed corporators in such anomalous relations. And it is certain that public policy is opposed to any tying up of capital where it has ceased to be productive, in order that debts may accrue to absorb it. Moreover, the very statement of the effect of dissolution of the corporation upon this guaranty, shows how inaccurate it must be to speak of the obligation created by it as constituting a "debt". A debt is the same, whether the debtor lives or dies, though in the latter contingency nothing may be realized; but here, in the event of corporate dissolution, nothing is received by the supposed creditor, and nothing is due him.

A contract the necessary construction of which would be that on which the plaintiff relies, and which would lead or tend to the consequences pointed out,—which would require dividends when honesty and good faith to the public would forbid, and public opinion condemn them, which would antagonize the positions of different classes of men engaged in the same joint undertaking, and preclude harmony of action and union of effort, precisely under those circumstances when harmony and union would be most essential, under which the corporation making it must almost inevitably be destroyed unless it should enjoy continuous prosperity, and which, under some circumstances, would make one class of persons having a voice in the control and management of the corporation interested in so controlling its means as to keep them as long as possible in an unproductive condition, until by a slow process they can absorb them to the prejudice of their associates,—must necessarily be opposed to public policy and void. And a contract which will bear any other reasonable construction could not, consistently with the rules of law, and with regard to what must be deemed the intent of the parties, that their contract should be just, reasonable and beneficial, have this construction put upon it.

We think the guaranty here in question will bear the construction that the preference stockholders shall be entitled to five per cent. semi-annual dividends when there are profits to pay them, and not otherwise. Probably if profits were not realized to the necessary amount in any one year, they would be entitled when they were realized, to have all arrears made up. *Henry v. Great Nor. Railway Co.*, 1 De Gex & Jones, 635; *Taft v. Hartford, etc., Railroad Co.*, 8 R. I. 334. This, we think, is what would be the general understanding of such a guaranty, and this is as far as the law would permit a corporation to go in guaranteeing dividends to its own members; and to this extent no rule of good faith or of public policy is in the way. An individual holding and selling stock might give a broader guaranty, but that has nothing to do with the questions arising upon this instrument.

There are two branches to the plaintiff's argument: the other being that if the guaranty is void as opposed to public policy, or if there was any defect of authority in the directors of the company issuing the preference stock without a previous assent of stockholders, then the money paid by the plaintiff to the company for the stock, is money which the company received to his use, and which therefore he may recover in this action. (Upon this it is sufficient to remark, that the guaranty properly construed is not void, but unobjectionable, and that if there was any defect in power in the directors to issue the stock, the corporation is not shown to have raised any question on the subject; and the recognition of the stock at the meetings of the corporation is fully shown.)

The ruling of the court below appears to us correct, and the judgment will be *affirmed*, with costs.

The other Justices concurred.¹

FOSTER v. NEW TRINIDAD LAKE ASPHALT CO., LTD.

1901. L. R. (1901) 1 Ch. Div. 208.

MOTION.

This was an application on behalf of debenture-holders and of a shareholder in the New Trinidad Lake Asphalt Company, Limited, which raised the question as to the proper method of dealing with an unexpected appreciation of assets. It was for an interim injunction to restrain the company and its directors from declaring or paying a dividend out of a sum of \$100,000, part of a sum of \$127,355, recently received from the New York and Bermudez Company, and

¹ See *Stringer's Case* (1869) L. R. 4 Ch. App. 475; *Cary v. Savings Union* (1874) 22 Wall. (U. S.) 38, 22 L. ed. 779; *Belfast &c. R. Co. v. Belfast* (1885) 77 Me. 445, 1 Atl. 362 (defining net earnings in detail); *Hubbard v. Weare* (1890) 79 Iowa 678, 44 N. W. 915; *McVity v. Albro Co.* (1904) 90 App. Div. (N. Y.) 109, 86 N. Y. S. 144.—Eds.

from treating the said sum of \$100,000 or any part thereof as available for distribution, or so distributing the same.

The matter being considered a pressing one, the application was made on short notice, but the balance-sheets for the year 1898, presented in May, 1899, and books of the company were put in evidence. The facts, as stated in the plaintiffs' affidavits, which were accepted by the Court for the purposes of this decision, were as follows:—

In 1894 an American company, the Trinidad Lake Asphalt Company, Limited (referred to in the affidavits as the "old company"), acquired the stock and bonds of the New York and Bermudez Company, and also a debt of \$100,000 due from the latter company to the old company and secured by promissory notes. In 1897 the defendant company, an English company, purchased the property and assets of the old Trinidad Company, including the debt for \$100,000 then due from the New York and Bermudez Company.

On December 31, 1899, the New York and Bermudez Company gave to the defendant company new promissory notes for \$127,355, being the amount of the said debt of \$100,000 with accrued interest thereon. The notes for this \$127,355 had recently been paid off, and the defendant company, through their directors, now proposed, without reference to the other business or assets of the defendant company, to treat the whole of that sum, amounting to 26,258L. 16s. in English currency, as assets available for dividends, and to distribute the same accordingly. It was also stated in one of the defendants' affidavits that on the balance-sheets of the company these promissory notes had never appeared as part of the assets, and that the only entry relating to them was in a journal entry, carrying them to the profit-and-loss account. * * *

Nov. 27. BYRNE, J., after stating the facts, continued:—This is the statement in the plaintiffs' affidavit, and it is not denied by the defendants, so that, although some discussion took place in argument upon the point, I have not now to consider whether or not the amount in question may properly be brought into the next profit-and-loss account, but simply whether or not the amount may be divided as profit, without regard to the present value of the ~~total capital~~ assets, and whatever the result of the year's trading may be. No question is raised as to so much of the sum as represents interest, the point at issue being as to the amount representing principal of the debt. There is no doubt that the debt formed part of the assets originally purchased by the defendant company, and as such, part of its original capital assets, but it is argued that as the debt was not regarded or treated as an asset of any value upon the purchase, and as it has not appeared in the former balance-sheet as part of the assets of the company, and as the only entry in relation to it in the books of the company is a journal entry carrying the notes to a profit-and-loss account, it ought to be regarded as a windfall in the nature of an unexpected profit, and as divisible accordingly amongst the shareholders. I cannot accept this view. Although the

agreement for sale does not enumerate the debt or notes in question in the schedule which purports, according to its heading, to be a statement of assets and liabilities of the old Trinidad Asphalt Company, that schedule is, as appears by clause 1 of the agreement, an enumeration of matters and things which the vendor warranted to be included in the property sold, or the equivalent in value thereof. Some of the items mentioned in the schedule may have been overvalued, some undervalued, and no doubt fluctuations in value of the assets have supervened, but the amount of this debt is a distinct item of the property purchased which has since been realized by payment. It appears to me that the amount in question is *prima facie* capital, and that I have no evidence which would justify me in saying that it has changed its character because it has turned out to be of greater value than had been expected. It was urged for the defendants that the amount applied in payment of the debt was money earned by the Bermudez Company by favour of the defendant company, and represents a profit which would otherwise have been earned by the defendant company, and, furthermore, that this money might have been applied by the Bermudez Company in payment of a dividend on the shares in that company, in which case the defendant company, as owning 9,842 shares out of a total of 10,000 in that company, would have received the greater portion as income. I am unable to follow this argument, as I do not see how for the purposes of the present motion, I can have regard to the fact that some other course of dealing by the debtor company would have left the debt still outstanding, and would have produced more income for the defendant company. I think that I ought to grant an injunction until judgment or further order to restrain the defendants from distributing the \$100,000 as dividend without reference to the other business or assets of the defendant company. I must not, however, be understood as determining that this sum or a portion of it may not properly be brought into profit-and-loss account or be taken into account in ascertaining the amount available for dividend. That appears to me to depend upon the result of the whole accounts for the year. It is clear, I think, that an appreciation in total value of capital assets, if duly realized by sale or getting in of some portion of such assets, may in a proper case be treated as available for purposes of dividend. This, I think, is involved in the decision in the case of *Lubbock v. British Bank of South America* (1892) 2 Ch. 198, cited with approval by Lord Lindley in *Verner v. General and Commercial Investment Trust* (1894) 2 Ch. 239, where he says: "Moreover, when it is said, and said truly, that dividends are not to be paid out of capital, the word 'capital' means the money subscribed pursuant to the memorandum of association, or what is represented by that money. Accretions to that capital may be realized and turned into money, which may be divided amongst the shareholders, as was decided in *Lubbock v. British Bank of South America*." If I rightly appreciate the true effect of the decisions, the question of what is profit available for

dividend depends upon the result of the whole accounts fairly taken for the year, capital, as well as profit and loss, and although dividends may be paid out of earned profits in proper cases, although there has been a depreciation of capital, I do not think that a realized accretion to the estimated value of one item of the capital assets can be deemed to be profit divisible amongst the shareholders without reference to the result of the whole accounts fairly taken.*

WILLIAMS v. WESTERN UNION TELEGRAPH CO.

1883. 93 N. Y. 162.*

EARL, J.— * * * The main contention was, that the stock dividend distributing upward of \$15,000,000 of stock among the stockholders of the Western Union Telegraph Company, was unauthorized and in violation of law, and whether it was or not is the principal matter for our determination upon this appeal. ?

The stock dividend was claimed to be in violation of chapter 18, part 1, title 4, section 2 of the Revised Statutes, which provides as follows: "It shall not be lawful for the directors or managers of any incorporated company in this State to make dividends excepting from the surplus profits arising from the business of such corporation; and it shall not be lawful for the directors of any such company to divide, withdraw, or in any way pay to the stockholders, or any of them, any part of the capital stock of such company, or to reduce the said capital stock without the consent of the legislature; and it shall not be lawful for the directors of such company to discount or receive any note or other evidence of debt in payment of any instalment actually called in and required to be paid, or any part thereof due or to become due on any stock in the said company; nor shall it be lawful for

* As to what constitutes profits out of which dividends may be declared, see also *Corry v. Londonderry etc. R. Co.* (1860) 29 Beav. 263, 30 L. J., Ch. 290, 7 Jur. (N. S.) 508; *In re London India Rubber Co.* (1868) L. R. 5 Eq. 518; *Lubbock v. British Bk. of South America* (1892), 2 Ch. Div. 198; *Hyatt v. Allen* (1874) 56 N. Y. 553, 15 Am. Rep. 449; *Miller v. Brodish*, 69 Iowa 278, 28 N. W. 594; *Estate of Geo. L. Oliver* (1890) 136 Pa. St. 43, 20 Atl. 527, 9 L. R. A. 421, 20 Am. St. 894; *Whittaker v. Amwell Nat'l Bk.* (1894) 52 N. J. Eq. 400, 29 Atl. 203; *Mobile & C. R. Co. v. Tennessee* (1894) 153 U. S. 486, 38 L. ed. 793, 14 Sup. Ct. 968.

"The general rule is that dividends can only be declared and paid out of net profits. In 1 *Morawetz on Private Corporations* (2d ed.), § 438, the rule is thus stated: 'The right to declare a dividend depends upon the state of the company's finances at the time when the dividend is declared. The question usually is, whether or not there would remain a net increase upon the original investment, after deducting from the assets of the company all present debts and making provision for future or contingent claims.'" *Lumpkin, J.*, in *Crawford v. Roney* (1908), 130 Ga. 515, 518, 61 S. E. 117. See *In re Haas Co.* (1904) 131 Fed. 232, 65 C. C. A. 218.—Eds.

* Only a portion of the opinion is given.—Eds.

such directors to receive or discount any note or other evidence of debt with the intent of enabling any stockholder in such company to withdraw any part of the money paid in by him on his stock; and in case of any violation of the provisions of this section the directors, under whose administration the same may happen, except those who may have caused their dissent therefrom to be entered at large on the minutes of the said directors at the time, or were not present when the same did happen, shall, in their individual and private capacities, jointly and severally, be liable to the said corporation and to the creditors thereof, in the event of its dissolution, to the full amount of the capital stock of the said company, so divided, withdrawn, paid out, or reduced, and to the full amount of the notes or other evidences of debt so taken or discounted in payment of any stock, and to the full amount of any notes or evidences of debts so discounted with the intent aforesaid, with legal interest on the said respective sums from the time such liability accrued; and no statute of limitation shall be a bar to any suit at law or in equity against such directors for any sums for which they are made liable by this section; provided this section shall not be construed to prevent a division and distribution of the capital stock of such company which shall remain after the payment of all its debts upon the dissolution of such company, or the expiration of its charter."

This dividend was condemned by the General Term of the Superior Court as a violation of that section. Our attention has been called to no other law forbidding or condemning a stock dividend, and in their allegations against it the counsel for the plaintiff rely mainly upon that section. After reading the numerous opinions that have been submitted to us and giving careful attention to all that has been said upon the subject, we are unable to perceive that that section has any bearing whatever upon the question we are to determine. The section was taken from the act chapter 325 of the Laws of 1825, which was entitled, "An act to prevent fraudulent bankruptcies of incorporated companies, to facilitate proceedings against them, and for other purposes." It was not part of the original revision, but was incorporated into the Revised Statutes by chapter 20 of the Laws of 1828. A careful reading of the section shows that it has reference only to the property capital of a corporation, and not to its share capital. The first clause prohibits dividends of property except from surplus profits. It is further provided that the directors of any corporation shall not divide, withdraw, or in any way pay to the stockholders or any of them, any part of the capital stock of such company, or to reduce the capital stock without the consent of the legislature. These provisions were intended to prevent the division, distribution, withdrawal and reduction of the property of a corporation below the sum limited in its charter or articles of association for its capital, but not to prevent its increase above that sum. The purpose was to prevent the depletion of the property of the corporation thereby endangering its solvency. All the other provisions of the

section show very clearly that such was the intention. Careful provision was made that the whole amount of capital stock should be paid in, and hence there was a prohibition against receiving a note or other evidence of debt in payment of any instalment actually called in and required to be paid; and in case the directors violated any of the provisions of the section they were made individually liable to the corporation and to its creditors, in the event of its dissolution, to the full amount of the capital stock of the company so divided, withdrawn or reduced. All these provisions show that it was the purpose of the legislature, by means of them, to create a property capital for the corporation, and then to keep that intact so as to secure the solvency of the corporation and its responsibility to its creditors. The "capital stock" in this section does not mean share stock, but it means the property of the corporation contributed by its stockholders or otherwise obtained by it, to the extent required by its charter. While the term "capital stock" is frequently used in a loose and indefinite sense, in this section and in legal phrase generally it means that and no more. In *State v. Morristown Fire Association* (3 Zab. 195), GREEN, Ch. J., said: "The phrase 'capital stock' is very generally, if not universally, used to designate the amount of capital to be contributed for the purposes of the corporation. The amount thus contributed constitutes the 'capital stock' of the company." In *Burrall v. Bushwick R. R. Co.* (75 N. Y. 211), Folger, J., defined "capital stock" as "that money or property which is put in a single corporate fund by those who by subscription therefor become members of a corporate body." In *Barry v. Merchants' Exchange Co.* (1 Sandf. Ch. 280), Vice-Chancellor Sandford said: "The capital stock of a corporation is like that of a copartnership or joint-stock company, the amount which the partners or associates put in as their stake in the concern." By loss or misfortune, or misconduct of the managing officers of a corporation, its capital stock may be reduced below the amount limited by its charter; but whatever property it has up to that limit must be regarded as its capital stock. When its property exceeds that limit, then the excess is surplus. Such surplus belongs to the corporation and is a portion of its property, and, in a general sense, may be regarded as a portion of its capital, but in a strictly legal sense it is not a portion of its capital, and is always regarded as surplus profits. The very section we are considering contemplates that there may be a surplus, and that such surplus may be divided. The surplus may be in cash, and then it may be divided in cash; it may be in property, and if the property is so situated that a division thereof among the stockholders is practicable, a dividend in property may be declared, and that may be distributed among stockholders. All such dividends diminish and deplete the property of the corporation, and that section was designed to prevent dividends of property which tended to deplete the assets of the company below the sum limited in its charter as the amount of its capital stock. But stock dividends never diminish or interfere with the property

of a corporation, and hence are not within the purview of that section. After a stock dividend a corporation has just as much property as it had before. It is just as solvent and just as capable of meeting all demands upon it. After such a dividend the aggregate of the stockholders own no more interest in the corporation than before. The whole number of shares before the stock dividend represented the whole property of the corporation, and after the dividend they represent that and no more. A stock dividend does not distribute property, but simply dilutes the shares as they existed before; and hence that section in no way prevented or related to a stock dividend. Such a dividend could be declared by a corporation without violating its letter, its spirit or its purpose. It is, therefore, clear that the directors of the Western Union Telegraph Company did not violate that section by the stock dividend which they declared; and if that dividend was illegal it must be because it was condemned by some other statute, or by some general principle of law or by public policy.

Our attention has been called to no statute, and we know of none in this State which prohibits a corporation from making a stock dividend. The legislatures in some of the States have, we believe, passed laws prohibiting such dividends; but in this State no such law has been enacted.

There is no public policy which, in all cases, condemns such dividends. Shares having been legally brought into existence may be distributed among the stockholders of a company. By such distribution no harm is done to any person, provided the dividend is not a mere inflation of the stock of the company, with no corresponding values to answer to the stock distributed. It may be that a distribution of stock gratuitously to the stockholders of a company based upon no values, a mere inflation, or, to use a phrase much in vogue, a watering of stock, would be condemned by the law. But when stock has been lawfully created and is held by a corporation, which it has a right to issue for value, then a stock dividend may be made, provided that the stock always represents property. It is conceded that the directors of the Western Union Telegraph Company could have issued this stock for money to be paid into its treasury. It could have issued it for property to be received by it for the purposes of its legitimate business. But here it is found that over and above its capital it possessed property actually worth upwards of \$15,000,000, and we know of no law that is violated, and no public policy that is invaded by issuing to the stockholders stock to represent that amount of property rather than in any mode to divide it up and distribute it among them. If it can issue stock in payment of property to be obtained by it as part of its capital for its legitimate uses, why may it not issue stock to its stockholders in payment for property in effect purchased of them and added to its permanent capital, and which they relinquish the right to have divided? So long as every dollar of stock issued by a corporation is represented by a

dollar of property, no harm can result to individuals or the public from distributing the stock to stockholders. (Here there was no fraud, no conspiracy, no unlawful combination, and we are bound, under the findings of the court at Special Term, to assume that all this was done in good faith; and we know of no principle of law, no public policy, and no statute that condemns a stock dividend under such circumstances.) (Howell v. The Chicago & Northwestern R. Co., 51 Barb. 378; Jones v. Terre Haute & Richmond R. R. Co., 57 N. Y. 196; Kenton Furnace, etc., Co. v. McAlpin, 5 Fed. Rep. 743; Attorney-General v. State Bank, 1 D. & B. Eq. Cas. 545; Minot v. Paine, 99 Mass. 101; Rand v. Hubbell, 115 id. 471; Brown v. Lehigh Coal & Nav. Co., 49 Penn. St. 270; Commonwealth v. Pittsburgh, Fort Wayne & Chicago R. Co., 74 id. 83; Terry v. Eagle Lock Co., 47 Conn. 141; Barton's Trust, L. R., 5 Eq. Cas. 239; Mills v. Northern R. of B. A. Co., L. R., 5 Ch. App. 621; Pierce on the Law of Railroads [2d ed.], 123.)

It is true that this dividend largely increases the capital stock of the company, but that is not against the policy of our laws. That cannot be against the policy of the law which the law expressly permits. There is no limit to the capital which business corporations in this State may have, and there is no limit in the law beyond which they may not increase their capital. All that can be required in any case is that there shall be an actual capital in property representing the amount of share capital issued. Indeed, so far as the solvency and responsibility of a corporation is concerned, they are increased by a stock dividend where it has a surplus of property to correspond to the amount of shares issued. In such case the surplus property is secured and impounded for the benefit of the creditors of the corporation and for the public, so that thereafter it can never be legally divided, withdrawn or dissipated in any way.

But if it can be conceived that this was a dividend of property within the meaning of the section of the Revised Statutes above set out, then what property did it divide? Not any portion of the capital of the company; that remained intact. After subtracting the dividend there remained to the company the full amount of its prior capital stock, to-wit: Property to the value of \$41,073,410. Such is the finding of the trial court, and that cannot here be disputed. The company had made surplus earnings which it could have divided, but instead of dividing them it had invested them in property to facilitate and enlarge its business; and such property was found to be worth \$15,526,590. That sum constituted its surplus. It was commingled with the other property of the company and used for corporate purposes. But it was not beyond the reach of the dividend-making power of the directors. They could reclaim it for division among the stockholders, and, if practicable, convert it into cash for that purpose. They could borrow money on the faith of it and divide that. They could issue to the stockholders certificates of indebtedness, redeemable in the future, representing their respective in-

terests in such surplus, thus, in effect, borrowing the same of the stockholders. Desiring to use the surplus and add it to the permanent capital of the company, and having lawfully created shares of stock, they could issue to the stockholders such shares to represent their respective interests in such surplus. In doing these things no law would be violated, the capital would be kept intact, and no stockholders or creditors would have any legal right to complain. All this, however, depends upon the finding of the trial court that the surplus is equal to the dividend. That finding is not open to criticism here. It was not disturbed at the General Term and therefore concludes us.

When a corporation has a surplus, whether a dividend shall be made, and if made, how much it shall be, and when and where it shall be payable, rest in the fair and honest discretion of the directors uncontrollable by the courts. (*Brown v. Monmouthshire R'y & C. Co.*, 4 Eng. L. & Eq. 118; *Rex v. Bank of England*, 2 Barn. & Ald. 620; *Jackson's Admr's. v. Newark Plankroad Co.*, 31 N. J. Law, 277; *Ely v. Sprague*, Clark's Ch. 351.) There is no statute which requires dividends in telegraph companies or in companies generally to be made in cash. Whether they shall be made in cash or property must also rest in the discretion of the directors. There is no rule of law or reason founded upon public policy which condemns a property dividend. The directors could convert the property into cash before a dividend and divide that. So the stockholders can take the property divided to them and sell it and thus realize the cash. Within the domain of law, it can make no material difference which course is pursued. If, however, a dividend be made payable in cash or payable generally, the corporation becomes a debtor, and must discharge such debt, as it is bound to discharge all its other debts, in lawful currency. It is true that a stockholder cannot be compelled to receive property divided to him. So he cannot be compelled to take a cash dividend. In case of his refusal to take a cash dividend, the corporation may retain it for him until he shall demand it. In case he shall refuse to take a property dividend, the corporation may retain it and hold it in trust for him, or possibly sell it for his benefit. If such a case shall ever arise, the courts will find some way to dispose of it. So this plaintiff cannot be compelled to accept the stock divided to him, and thus incur the possible liability which it may impose upon him as a stockholder. In case of his refusal, the corporation will find some way to deal with the stock which the law will sanction, but which need not now be pointed out.

We have no occasion to scrutinize the motives of the defendants. The trial judge refused to find the alleged fraud and conspiracy, and his finding concludes us. In his opinion he said: "I have also found that the other allegations of fraud and conspiracy made in the complaint against the defendants and others were not proved on the trial. One of the very able counsel for the plaintiff, in his

argument at the close of the trial in this case, said that he was not going to lament the fact that he had failed to show such combination, that he had not been able to prove certain things by the defendants;" and the opinion of the court at the General Term is to the same effect: "The complaint, among other things, charges that the corporate action complained of was the result of a fraudulent conspiracy on the part of the individual defendants, but the allegations in that respect were not sustained by the proof at the trial, nor has there been an argument made in their support upon the present appeal."

We are, therefore, of opinion upon the facts, found at Special Term, that the stock dividend was authorized by law and, therefore, valid.⁴

KING v. PATERSON AND HUDSON RIVER R. CO.

1861. 29 N. J. L. 504.

IN ERROR to the Supreme Court.

The opinion of the court was delivered by THE CHANCELLOR.—The action is brought to recover the amount of two dividends, declared in January and July, 1857, upon two hundred shares of the capital stock of the corporation owned by the plaintiffs. The dividends were made payable at the branch office of the Ohio Life Insurance and Trust Company, in the city of New York, the trust company being appointed registers of the railroad company to transfer stock and to pay dividends. Notice of the dividends and of the time and place of payment was published in a newspaper printed and published in the city of New York. The money to pay the dividends was deposited by the defendants in the office of the trust company, before the day of payment of each of said dividends, ready to be paid to the plaintiffs on their application. The money was left in the hands of the trust company until the 24th of August, 1857, when the company failed, and the money was lost.

After a dividend is declared, all community of interest in relation to such dividend, as between the stockholders themselves and between the stockholders and the corporation, is at an end. The right of a party to whom the dividend is payable is recognized as a separate and independent right, which may be enforced as against the corporation. *Davis v. The Bank of England*, 5 Barn & Cress. 185;

⁴See *Brown v. Lehigh Coal & Navigation Co.* (1865) 49 Pa. St. 270; *Terry v. Eagle Lock Co.* (1879) 47 Conn. 141, esp. 163-166; *Kaufman v. Charlottesville Woolen Mills Co.* (1896) 93 Va. 673 at 675, 25 S. E. 1003; *Union & Co. Trust Co. v. Taintor* (1912) (Conn.) 83 Atl. 697; *DeKoven v. Alsop* (1903) 205 Ill. 309, 68 N. E. 930, 63 L. R. A. 587 ("A stock dividend is lawful when an amount of money or property equivalent in value to the full par value of the stock distributed as a dividend has been accumulated and is permanently added to the capital stock of the corporation").—Eds.

Coles v. The Bank of England, 10 Ad. & E. 437; Carlisle v. South Eastern Railway Co., 6 English Rail. Cas. 685; 1 Shelf. on Rail. 205.

This principle was fully recognized in *Le Roy v. The Globe Insurance Co.*, 2 Edw. Ch. R. 657, although the precise character of the relation subsisting between the stockholder and the corporation in respect to the dividend was not clearly defined. In the opinion of the Vice Chancellor, if payment of the dividends declared is withheld by a solvent corporation, payment may be enforced at the instance of the stockholders by mandamus, by suit at law on behalf of individual stockholders for the payment of the money, or by bill in equity to obtain possession of the money as a trust fund, which the corporation were bound to distribute, and over which they had no other control. In that case, the company being insolvent, it was held that the money appropriated and set apart for distribution among the stockholders by way of dividend became a trust fund in the hands of the corporation, to which the stockholders, as individuals, had acquired vested rights, and that they consequently were entitled to the fund in preference to the creditors of the corporation.

In *Kane v. Bloodgood*, 7 Johns. C. R. 90, Chancellor Kent held that an action at law for money had and received would lie by a stockholder against a corporation for the recovery of a dividend, and that it was not such an express trust as would take the case out of the statute of limitations.

The true principle is, that the dividend, from the time that it is declared, becomes a debt due from the corporation to the individual stockholder, for the recovery of which, after demand of payment, an action at law may be maintained. *State v. Balt. and Ohio Railway*, 6 Gill 363; *Phil., Wil. and Balt. Railway v. Crowell*, 28 Penn. St. Rep. 329; *Ohio City v. Cleveland and Toledo Railway*, 6 Ohio St. Rep. 329.

Like any other debt, it may be set off against the debt of the stockholder to the corporation. *Bates v. New York Insurance Co.*, 3 Johns. Cas. 238; 12 Serg. & R. 77.

It may be, by banking corporations, sometimes carried to the general account of the stockholder with the corporation, and is thus applied in adjusting balances between the parties or in satisfying the claims of the corporation against the stockholder. They thus act in the character not of trustees, but of debtors. The fund is dealt with not as a trust fund, but as money due. And why should it not be so regarded? What principle is violated? Does not sound policy require that the relation between the stockholder and the corporation in relation to the dividend should be simply that of debtor and creditor; that the stockholder should have his remedy at law, and that the corporation should be permitted to apply it by way of set-off to satisfy demands against the stockholder?

Why is the case distinguishable in principle from that of a stockholder who is also a depositor? The dividend and the deposit are

alike debts due from the corporation to the stockholder. Both are in the keeping and under the control of the corporation with the assent and concurrence of the stockholder. It has been repeatedly decided that an action lies for a deposit by a depositor against a corporation after demand. The fact that he is a member of the corporation cannot vary the principle. *Downes v. The Phoenix Bank of Charlestown*, 6 Hill 297; *Watson v. The Phoenix Bank*, 8 Metc. 217.

In a limited sense, the deposit and the dividend in the hands of the corporation are alike trusts. Every deposit is a direct trust. Every person who receives money to be paid to another, or to be applied to a particular purpose, to which he does not apply it, is a trustee. *Kane v. Bloodgood*, 7 J. C. R. 110; *Scott v. Surman*, Willes 404. In this limited sense, and in no other, the corporation is a trustee of the dividend unpaid to the stockholder.

The debt is strictly demandable and to be paid at the office of the corporation. Admitting the right of the corporation to make it payable elsewhere, it must be done at the risk of the corporation. The debtor has no right, without the consent of the creditor, express or implied, to intrust a third party with the fund for the purposes of payment. The trust company with whom the funds were deposited for payment was the agent of the corporation, not of the stockholders; of the debtor, not of the creditor. If the agent prove faithless, or the fund is lost in his hands, the loss must fall upon the owner. The deposit was made in the name of the corporation, and was subject to their control. There is nothing in the special verdict that shows a consent, express or implied, on the part of the plaintiffs to their funds being intrusted to, or deposited with, the the Ohio Life and Trust Company.

Strong considerations in support of this conclusion may, perhaps, as was urged upon the argument, be derived from the peculiar provisions of the charter of the railroad company, as well as from the policy of the law, which would deny to a corporation, within this state, the right to deposit moneys due to its creditors in the hands of a foreign corporation. But the decision is designedly based upon the sole ground, (that after a dividend is declared, it becomes a debt due from the corporation to the stockholder as an individual, and that the selection of an agent for the payment of that debt by the debtor without the concurrence of the creditor must be at the risk of the debtor alone.) The fund remains the property of the corporation until payment is made. If a loss is sustained, it falls upon the owner.

The judgment must be affirmed.

For affirmance.—The Chancellor, the Chief Justice, and Judges Brown, Combs Cornelison, Kennedy, Risley, Swain, and Wood.

For Reversal.—None.*

* In the court below, Haines, J. said: "It is a clear proposition, that a dividend declared of the earnings of a company becomes thereupon the indi-

HUNT, RECEIVER, v. O'SHEA, ASSIGNEE.

1899. 69 N. H. 600, 45 Atl. 480.

ASSUMPSIT AND PROBATE APPEAL, to recover for the same cause of action. Facts agreed. The plaintiff is the receiver of the People's Fire Insurance Company, and as such, on July 1, 1894, was the holder of one hundred and fifty shares of the capital stock of the Laconia Car Company, as collateral for a note which has not been paid. The Car Company before that time had legally declared a dividend payable on that date, which on this particular stock has not been paid.

January 25, 1897, proceedings were instituted upon which the Car Company were decreed insolvent debtors, and the defendant was appointed their assignee. The plaintiff's claim for this dividend was allowed in the probate court, but that court denied his motion to order it paid in full.

YOUNG, J.—This court has no original jurisdiction of claims against the estate of an insolvent debtor (P. S., c. 201, s. 1), so the action of assumpsit must be dismissed; for the defendant has no money in his hands which equitably belongs to the plaintiff. Simply declaring a dividend does not create a trust fund. *Lowne v. Insurance Co.*, 6 Pai. 482. To create such a fund, some specific sum of money must be set apart for the purpose of paying the dividend. Until this is done, the relation of the corporation to its stockholders in respect to dividends is that of debtor and creditor. *King v. Railroad*, 29 N. J. Law 82; 1 Mor. Corp., s. 445. No sum of money having been set apart to pay this dividend, and the claim not being one of those named in s. 32, c. 201, P. S., the appeal should be dismissed, and judgment entered for the defendant in the action at law.

Case discharged.

All concurred.*

vidual property of the stockholder, to be received by him on demand. It is a severance from the common fund of the company of so much for the use and benefit of each corporator, in his individual right, which may be demanded by him, and if refused, become the subject of an action for money had and received to his use." (29 N. J. Law, at p. 87.)

See *Cratty v. Peoria Law Library Assn.* (1906) 219 Ill. 516, 76 N. E. 707; *McLaran v. Crescent Planing Mill Co.* (1906) 117 Mo. App. 40, 93 S. W. 819; *Camden Nat. Bank v. Fries-Breslin Co.* (1906) 214 Pa. St. 395, 63 Atl. 1022.

That accumulated profits are not the property of the shareholders until the declaration of dividends, see *Stanwood v. Sterling Metal Co.* (1903) 107 Ill. App. 569.—Eds.

* *Lowne v. Amer. Fire Ins. Co.* (1837) 6 Paige Ch. (N. Y.) 482, *Accord.* Cf. *LeRoy v. Globe Ins. Co.* (1836) 2 Edw. Ch. (N. Y.) 657 (setting aside of specific fund); *Matter of LeBlanc* (1878) 14 Hun (N. Y.) 8, 4 Abb. N. C. 227, (affd. 75 N. Y. 598); *Searles v. Gebbie* (1906) 115 App. Div. 778, 101 N. Y. S. 199 (affd. 190 N. Y. 533).

Where a specific fund has been set apart for the payment of a dividend

FORD v. EASTHAMPTON RUBBER THREAD CO.

1893. 158 Mass. 84, 32 N. E. 1036.

CONTRACT, for money had and received. At the trial in the Superior Court, without a jury, before Aldrich, J., there was evidence tending to show that the plaintiff on June 16, 1891, owned fifty-two shares of the capital stock of the defendant company, of the par value of one hundred dollars per share; that on that day the directors passed the following vote, namely, "That a dividend of 20 per cent be paid to stockholders of this date, payable Tuesday, June 23d, 1891;" that on said June 16th the annual meeting of stockholders of the company for the election of directors was held immediately after the meeting of directors, according to custom, and duly elected five directors, as provided by the by-laws of the company, two only of the old directors being re-elected, and no director being re-elected who voted for the twenty per cent. dividend, though the two who were re-elected were present at the meeting when it was voted; and that on said June 16th, as soon as the stockholders' meeting adjourned, the directors elected and re-elected thereat met, qualified, organized for the year, and passed the following votes: "That the vote passed by the directors of this company this day declaring a dividend of 20 per cent on the capital stock of the company, payable Tuesday, June 23d, 1891, be reconsidered and rescinded; the same is hereby rescinded. That a dividend of six per cent., payable June 23d instant to stockholders of record this day, be declared in place of the dividend voted at earlier meeting of this board this day." It also appeared that no money was set aside or provided to pay said dividend of twenty per cent., but the company had ample means and facilities for paying the twenty per cent. dividend; that always before money had been provided to pay a dividend before it was declared; that money to pay said six per cent. dividend was provided after the meeting and before said 23d of June by borrowing, and the same was set aside and deposited in bank therefor; that the treasurer sent the check of the defendant on the bank where the money was deposited to each stockholder of record of said June 16th to pay the dividend on his stock at six per cent., including the plaintiff, on said 23d June, 1891; and that the plaintiff declined to accept the check, and returned the money to the treasurer. It further appeared in evidence that no stockholder of the defendant had been paid the twenty per cent. dividend for June, 1891; that a majority of the stockholders had accepted the

declared, and corporate bankruptcy follows, *held*, "the stockholders are not required to go in pro rata with the general creditors for such unpaid dividends, but may proceed as against a trustee on account of such trust fund and recover the whole of their pro rata thereof." *McLaran v. Crescent Planing Mill Co.* (1905) 117 Mo. App. 40, at p. 48, 93 S. W. 819. *Matter of LeBlanc* (1878) 14 Hun (N. Y.) 8, 4 Abb. N. C. 227, (affd. 75 N. Y. 598), *acc.*—Eds.

dividend of six per cent. paid by checks as aforesaid on June 23, 1891, in full; that the plaintiff, by his attorney, by letter of June 30, 1891, demanded payment of the twenty per cent. dividend from the defendant; and that the plaintiff made no objection to the check of the defendant sent him to pay the dividend of June 16, 1891, except that it was for a dividend of six per cent., instead of twenty per cent.

The defendant asked the court to rule that the directors elected on June 16 had a right on that day to rescind the vote whereby the twenty per cent. dividend was declared payable at a future day; and that the plaintiff could not recover. The judge declined so to rule, ordered judgment for the plaintiff, and reported the case for the determination of this court. If the refusal to rule and order of judgment were correct, judgment was to be affirmed; otherwise, judgment was to be ordered for the defendant.

FIELD, C. J.—It seems to be settled that, when a dividend has been fully declared, the corporation thereby manifests its intention that the amount of the dividend should be considered as having been separated from the other property of the corporation, and as having become the individual property of the stockholders, and that therefore, when the dividend becomes payable according to the terms of the vote declaring it, each stockholder has a right to demand payment of the proportional part of the dividend which belongs to his shares of stock, and to sue the corporation for it, if it is not paid on demand. In some cases money or other property equal to the whole amount of the dividend declared has been specifically set apart as a fund appropriated to the payment of the dividend, and the stockholders have been regarded as the *cestuis que trust* of this fund, each entitled to his share. In other cases, the corporation has credited the stockholders with the amount of their shares of the dividend, and the stockholders have assented to this, and the amount so credited has been regarded as a debt of the corporation to the stockholders; or the corporation has paid to some of the stockholders their shares of the dividend, and has refused to pay anything to the others, and it has been held that the corporation must pay all alike. See *Beers v. Bridgeport Spring Co.* 42 Conn. 17; *State v. Baltimore & Ohio Railroad*, 6 Gill, 363; *King v. Paterson & Hudson River Railroad*, 5 Dutch. 504; *Jermain v. Lake Shore & Michigan Southern Railway*, 91 N. Y. 483; *Hopper v. Sage*, 112 N. Y. 530; *Jackson v. Newark Plankroad Co.* 2 Vroom, 277; *Wheeler v. Northwestern Sleigh Co.* 39 Fed. Rep. 347. When a dividend has been declared payable at a definite future time, but no fund has been set apart for the payment of the dividend, and the corporation meanwhile becomes insolvent, whether the stockholders to the extent of their proportions of the dividend should share ratably with the creditors of the corporation in its property has not, so far as we know, been recently considered, but the decision in *Lowne v. American Ins.*

Co. 6 Paige, 482, is that they should. The setting apart of a fund to pay a dividend has been held to give a lien upon it to the stockholders, which they can enforce to the exclusion of the general creditors of the corporation. In *re Le Blanc*, 14 Hun 8, and 75 N. Y. 598. *Le Roy v. Globe Ins. Co.*, 2 Edw. Ch. 657. The English Companies' Act, 1862, (25 & 26 Vict. c. 89, § 38, cl. 7), provides that "no sum due to any member of a company, in his character of a member, by way of dividends, profits, or otherwise, shall be deemed to be a debt of the company, payable to such member in a case of competition between himself and any other creditor not being a member of the company; but any such sum may be taken into account, for the purposes of the final adjustment of the rights of the contributories amongst themselves." Upon these questions, however, we desire to express no opinion.

It has been argued that there is no consideration for the promise of a corporation to pay a dividend to its stockholders, but we think that the doctrine of consideration applicable to a simple contract between persons having no fiduciary relations to each other is not applicable to such promise. It is the object of a private business corporation to make money for its stockholders, and, under our laws, it is ordinarily the duty of the directors from time to time to declare dividends out of the net earnings, if there are any, and it must be left largely to the discretion of the directors to determine when and for how much such dividends should be declared. The whole property of the corporation is held on a sort of trust for the stockholders, and the directors are, in a general sense, the managers; and when a dividend is declared by the directors, the declaration is a determination by a body authorized to make it that the amount of the dividend should be taken from the property of the corporation and paid over to the stockholders. The cause of action of each stockholder against the corporation for non-payment of the dividend does not arise from any actual contract between the corporation and its stockholders, but from the nature of the organization, and the relation of the stockholders to the corporation and its property. Unless the rights of creditors intervene, or the corporation is enjoined from paying the dividend, on the ground that the dividend has not been earned, or on some other ground, the amount of the dividend, after it has been declared and has become payable, is considered as property held by the corporation for the use of the stockholders individually, and the stockholders may recover their shares as money or property had and received to their use. We have been able to find little or no authority on the precise question involved in this case, namely, whether, after a dividend has been duly declared by a vote of the directors, but payable at a future time, the vote can be rescinded at a subsequent meeting of the directors, held before the time at which the dividend becomes payable according to the vote, when the fact that a dividend has been declared has not been made public, or in any manner com-

municated to the stockholders, and when no fund has been set apart for the payment of the dividend. On principle, we do not see why the directors may not rescind such a vote, under the circumstances stated. By the vote no specific property passed to the stockholders. If the vote be regarded as a declaration of trust in favor of the stockholders, it could be revoked before it was communicated to them or any property was identified and set aside for them. Indeed, cases may easily be supposed of such a change in the affairs of a corporation, between the time when a dividend is declared and the time when it becomes payable, as to make the exercise of such a power by the directors useful, if not necessary, for the successful continuance of the business of the corporation. It appears in the present case that the meeting of the new directors at which the vote was rescinded was held after the annual meeting of the stockholders, but on the same day as the meeting of the directors at which the vote was passed, which was held just before the meeting of the stockholders; and that at the meeting of the stockholders "the president did not, as had for many years been the custom, announce that any dividend had been declared, or promulgate the same to the stockholders;" and it does not appear that any of the stockholders, except the directors, knew of the original vote, or that any of the stockholders had made any contracts, incurred any liability, or done anything relying on the vote. It also appears that no fund was distinctly set apart for the payment of the dividend before the vote was rescinded. As the passage of the vote did not constitute an actual contract of the corporation with its stockholders, but was merely a mode of dividing the earnings of the property of the corporation among the stockholders, we are of opinion that before the division had been actually made, and before the position of the stockholders had been changed in reliance on the vote,—certainly before the passage of the vote had been made public, or communicated to the stockholders,—it was within the power of the directors, at a meeting subsequent to that at which the vote was passed, to rescind it. In this action at law, we cannot supervise the exercise of this power by the directors,

*Judgment for the defendant.*¹

¹"Ford v. East Hampton Rubber Thread Co., 158 Mass. 84, is cited and relied upon by appellant as authority for the action of the board of directors in rescinding the dividend. * * * The decision of that case can only be sustained upon the theory that the declaration of the dividend did not create a debt to the stockholders, for if a debt was thereby created, it is preposterous to say that such debt can be cancelled by the action of the debtor without the consent of the creditor. In fact, we understand the opinion, inasmuch as it is there asserted that 'the passage of the vote did not constitute an actual contract of the corporation with the stockholder,' as holding that the declaration of the dividend did not create a debt; and if this be its holding, it stands out boldly, single and alone in this country against an unbroken line of cases and overwhelming weight of authority that we are not at liberty to disregard, were we so inclined, and we are not." Norton, J. in McLaran

HOPPER v. SAGE.

1889. 112 N. Y. 530, 20 N. E. 350.

APPEAL from judgment of the General Term of the Superior Court of the city of New York in favor of plaintiff, entered upon an order made the first Monday of June, 1887, which overruled defendant's exceptions and directed judgment upon a verdict.

The action was brought to recover damages for alleged breach of contract.

On the 23d of May, 1878, the defendant for a valid consideration made an agreement with the plaintiff's decedent, of which the following is a copy:

"A. 3099.

New York, May 23, 1878.

"For value received, the bearer may deliver me, on one day's notice, except last day, when notice is not required, five hundred (500) shares of the common stock of the Chicago and Northwestern Railway Company at forty-nine (49) per cent., any time in thirty (30) days from date.

"The undersigned is entitled to all dividends or extra dividends declared during the time.

"Expires 1.3-4 o'clock P. M.

"RUSSELL SAGE."

On the 16th day of May, 1878, the board of directors of the above-named company, by resolution, declared a dividend on its capital stock of three per cent., both on the preferred and common stock, payable at the office of the company in New York on the 27th of June, 1878, and the transfer books were to be closed for the purpose of the dividend on Tuesday, June 18th, and reopened on Saturday, June 29, 1878. It was admitted, as a fact, upon the trial, subject to objection as to the materiality thereof, that the following rule was in force during the year 1878, upon the Stock Exchange in New York, viz.: "On the day of the closing of the transfer books of any stock for a dividend, transactions in such stock for cash shall be 'dividend on' up to the time officially designated for the closing of the books; all transactions other than for cash shall be 'dividend off' after a quarter past two o'clock P. M., or after the closing of the books, should they close before that hour." It was also admitted, subject to the same objection, that in conformity to the above rule and the resolution above-named declaring a dividend, the stock of the Chicago & Northwestern Railway was on June 18, 1878, quoted and dealt in upon the Stock Exchange, "dividend off."

On the twenty-second day of June, before 1:30 P. M. of that day, the plaintiff's decedent tendered five hundred shares of the com-

v. Crescent Planing Mill Co. (1905) 117 Mo. App. 40, at 50-51, 93 S. W. 819.

See Beers v. Bridgeport Spring Co. (1875) 42 Conn. 17.—Eds.

mon stock of the above-mentioned railway to the defendant, at his office in the city of New York, and demanded payment therefor at the rate of \$49 per share. The defendant refused to give that amount, but offered to receive and pay for the stock at the rate of \$46 per share, which the plaintiff's decedent refused to take, and notified the defendant that he should hold him for the difference between forty-nine and the market price, which was then forty-six. The defendant based his refusal to pay more than forty-six upon his alleged right to receive the dividend of three per cent on the common stock of the railway, which had been declared on the sixteenth of May, and which was payable on the 27th of June, 1878. The agreement, or, as it is termed in this case, the "put," was purchased of the defendant at his private place of business in New York, by a broker on behalf of plaintiff's decedent, and such broker, so far as appears, was not a member of the Stock Exchange. There was no disputed question of fact in the case, and the trial judge ordered a verdict to be entered for the plaintiff for the difference between the price agreed to be paid (\$49 per share) and the market price of the stock on the day when the tender was made, June 22, 1878, which price was \$46 per share, together with interest thereon from the day of such tender. * * *

PECKHAM, J.—The only question in this case is as to whether the defendant was entitled to insist upon his claim to the dividend on the common stock of the railway which had been declared on the 16th of May and was payable on the 27th of June, 1878. It has been held a number of times in this court that when a dividend is declared it belongs to the owner of the stock at that time, but that until such declaration the profits form part of the assets, and an assignment by a stockholder before such declaration carries with it his proportional share of the assets, including all undeclared dividends. This is so in regard to dividends declared, but which are payable at a future time, and such dividends belong to the owner of the stock when declared. The declaration of the dividend is in legal contemplation a separation of the amount thereof from the assets of the corporation, which holds such amount thereafter as the trustee of the stockholder at the time of the declaration of the dividend. In the absence, therefore, of any provision in a contract of sale and purchase of stock, outside of and not subject to the rules of the Stock Exchange, the law declares that such a contract gives the dividends to the owner of the shares when the dividends were declared. This rule was announced in *Boardman v. Lake Shore & M. S. Railway Co.* (84 N. Y. 157), *Jermain v. Same Defendant* (91 id. 483, 492) and in *Matter of Kernochan* (104 id. 618).

On looking at the contract in question, it is seen that the parties did make some provision as to dividends, and it was agreed that the defendant was to be entitled to all dividends or extra dividends declared during the time of its running, that is, for thirty days from

the date thereof, which was May 23, 1878. But that provision did not include the case of a dividend which had already been declared, and as to that dividend the contract was silent, and the law itself fixes the ownership thereof just the same as if it were thus provided in so many words in the contract. To overcome this result the counsel for the defendant endeavored in many and various ways to show that, by usage of the Stock Exchange, a person situated as was the defendant with reference to this stock and under precisely the same liability as the defendant, under the contract in question, was entitled to the dividend which had been declared, and which each party to this action now claims. All the various offers to prove facts, and all the various questions asked of different witnesses had this one result for their object, which was to change the law on the subject by reason of this custom or usage claimed to be prevalent on the New York Stock Exchange.

We think the learned trial judge correctly refused to permit evidence of this nature to be given. Usage and custom cannot be proved to contravene a rule of law or to alter or contradict the express or implied terms of a contract free from ambiguity, or to make the legal rights or liabilities of the parties to a contract other than they are by the terms thereof. When the terms of a contract are clear, unambiguous and valid, they must prevail, and no evidence of custom or usage can be permitted to change them. * * *

The evidence offered in this case would have been inconsistent with the rules of law and would have contradicted the plain terms and legal effect of the contract. This is not a case where, by the terms of the contract made between members of the Stock Exchange, its rules and regulations are to control in its interpretation and obligations. Nor was it made under such circumstances that those rules and regulations could have any legal effect. The contract was made at the office of the defendant and by a broker for plaintiff's decedent, who as to this contract, at all events, was not acting as a member of the Stock Exchange, and, so far as the case shows, he was not a member thereof.

There was no error committed on the trial, and the judgment entered upon the verdict for the plaintiff should be affirmed, with costs.

All concur.

*Judgment affirmed.**

* But see *Burroughs v. North Carolina R. Co.* (1872) 67 N. C. 376, 12 Am. Rep. 611, *contra*.

In *Bright v. Lord* (1875) 51 Ind. 272, 19 Am. Rep. 732, Biddle, C. J. said: "From the authorities and upon principle, we think the rule may be deduced, that whoever owns the stock in a corporation at the time a dividend is declared owns the dividend also, and a sale of the stock afterwards will not carry the dividend with it, though it may not be paid, or payable, until after the sale." And see *Wheeler v. Northwestern Sleigh Co.* (1889) 39 Fed. 347; *Elliott on Private Corps.*, (4th ed.) secs. 405, 412.

In *Steel v. Island Milling Co.* (1906) 47 Ore. 293, 83 Pac. 783, *held* that a corporation which had paid a dividend on stock to a person appearing

RAYNOLDS v. DIAMOND MILLS PAPER CO

1905. 69 N. J. Eq. 299, 60 Atl. 941.*

STEVENSON, V. C.—(Orally).

The bill is filed to secure two objects: One of these objects is to secure for all the stockholders of the defendant corporation, individually and severally, the benefit of a dividend, a distribution to be made to them severally and respectively of at least a portion of the accumulated profits of the corporate business. This remedy is one which is sought on behalf of each stockholder as an individual and the natural defendant in the proceeding is the corporation, the stockholders collectively, taken as a body, engaged not in individual pursuits, but in the pursuit of the corporate business for the common benefit of all. The effect of the declaration of a dividend, whether made voluntarily by a corporation through its board of directors or made compulsorily by the decree of a court of equity, is at once the establishment of a debt due from the corporation to each stockholder, which debt may be sued for in a court of law. The interests of the individual stockholder who prosecutes this sort of an action and the interests of the corporation, the stockholders collectively, who defend it, are plainly hostile. The individual stockholder is enriched and the stockholders collectively, the corporation, is, to the extent of the dividend, impoverished and crippled in its operations. * * *

And first, the complaint in the bill that the defendant corporation and its directors are unreasonably and wrongfully withholding the profits, piling them up, instead of distributing them, or distributing a portion of them, in the form of a dividend to the stockholders. The corporation was organized in the year 1894 with a capital stock of \$300,000. For some time past the entire capital stock has consisted of about \$275,000 of common stock and about \$25,000 of preferred stock, as I recall the figures. The preferred

on its books as owner, after the corporation had received notice of the transfer of the stock to a third person, was liable to said third person for the amount of the dividend, though at the time the dividend was declared the corporation had no notice and though the amount of the dividend had been immediately placed to the stockholder's credit on its books. Said Bean, Ch. J.: "If the corporation, without notice of the transfer or assignment of the dividend, had paid the same to the apparent holder of the stock, it would be discharged, but after such notice it was bound to pay the true owner." (p. 297)

As to the right to dividends between life-tenant and remainderman, see *Union &c. Trust Co. v. Taintor* (1912) 83 Atl. (Conn.) 697; *De Koven v. Alsop* (1903) 205 Ill. 309, 68 N. E. 930, 63 L. R. A. 587, and notes, 4 Columbia Law Rev. 130, 7 id. 344, 11 id. 556; *Minot v. Paine* (1868) 99 Mass. 101, 96 Am. Dec. 705; *Gray v. Hemenway* (1912), 98 N. E. (Mass.) 789; *McLouth v. Hunt* (1897) 154 N. Y. 179, 48 N. E. 548, 39 L. R. A. 230; *Earp's Appeal* (1857) 28 Pa. St. 368; *Gibbons v. Mahon* (1890) 136 U. S. 549, 10 Sup. Ct. 1057, 34 L. ed. 525.—Eds.

* Only portion of the opinion is given.—Eds.

stock draws seven per cent. annual dividends and is a small factor in the case, and the dividend has been regularly paid. The real question relates altogether to the claim that greater dividends should be paid and should have been paid for the year 1903-1904 on the \$275,000 of common stock. * * *

We now come to the question whether, apart from the statute, a case is here presented in which a court of equity should intervene and take the place of the board of directors and order a dividend to be declared, create a debt due from the corporation to these stockholders as individuals, for which they can maintain actions. This work of examining the situation of a great business corporation owning large plants, mills and machinery, and with large business transactions on its hands, by a court of equity, in order to find out whether dividends are being unfairly and unjustly and unreasonably withheld from the stockholders, is an exceedingly difficult task. Perhaps the rule has not been correctly formulated as yet, which controls the court of chancery in the exercise of its general equity jurisdiction apart from any statute, in endeavoring to perform this work. I am fully satisfied that where there is no charge of bad faith, no charge of fraud, but the charge is that the directors are unreasonably refraining from declaring a dividend, that it is unfair to the stockholders that there should not be a partial distribution, the court should not intervene if there is any room for doubt. Perhaps it would be more accurate to say the court ought not to take the place of the board of directors and control this business which is committed to their discretion, unless the case is perfectly plain. Now, in this case, there is no charge of bad faith against these directors. I think I might say that it is admitted that the managers of this corporation are men of integrity and ability, and that they have conducted the business of this corporation and built it up from a very small beginning until now it has assets of between \$500,000 and \$600,000, and seems to be in a very substantial financial position, with great skill. They began, as I said, in 1894, with nominally \$300,000, and now they have not quite doubled the assets—not quite doubled the difference between assets and liabilities, I think. They have made large profits during the last three or four or five years, and have steadily extended, acquired more mills and more machinery, and this policy of expansion culminated in 1903 in the purchase of a new mill at Saugerties, New York, in which \$133,000 was expended.

I shall not undertake to discuss in this way without having the figures and tables before me which were prepared so fully by counsel and which were so helpful to the court, the minutiae of the situation of this corporation in 1893 and 1894 and at the present time, but my conclusion is that no case is presented under the general equity power of the court in which an equity judge should intervene and direct the distribution of profits in the form of dividends to these stockholders, setting aside the action or determination of the

board of directors. This conclusion, however, is based upon the view which I entertain of the condition of the corporation and its business in 1903 and 1904, which is the period during which the bill alleges the dividends should have been declared, and at the present time. An entirely different conclusion might be proper and might be the only proper conclusion one year or two years from the present time. In the case of *Laurel Springs Land Co. v. Fougeray*, 50 N. J. Eq. (5 Dick.) 756, Mr. Justice Garrison, speaking for the court of errors and appeals, indicates that under the general equity power of this court, the court is not without control over a corporation where the directors roll their profits into their business year after year until the great snowball has been magnified twenty diameters. The intimation is distinctly made that a time will come when it is not fair to the stockholders, even though the directors may be acting in good faith, to indefinitely extend the corporate business. We start here in this case in 1894—we do not go back twenty years earlier when the original capital was \$8,000—but we start here in 1894 with a capital of \$300,000. The rolling-in process has not yet doubled the capital, but if this process keeps on indefinitely through eight or ten more years, until, instead of having less than \$600,000 imperiled in this business the corporation has several millions and desires to own almost all the paper mills in the country, then a very different question would be presented. [There must come a time, it seems to me, when it is unreasonable for directors to pursue a policy of expansion, but I cannot see that the proofs indicate that that point has been reached in this particular instance.] It is a matter of common knowledge that all great industries during the last twenty years, in order to their preservation, have been obliged to expand. It is a matter of common knowledge that a paper mill that was a fortune to a man thirty or forty years ago might by itself be a worthless asset to that man's grandson to-day. In order to keep that mill alive, in order to enable the business to be prosecuted advantageously and with profit, it might be necessary now to have four or five such mills so as to secure an enormously increased product. It is a matter of common knowledge that thirty or forty years ago the profit on every pound or yard or any other unit of measure was enormously greater than it is to-day, and therefore, in order to conduct one of these large manufacturing businesses profitably, the output has to be very much greater than of old. Well, I cannot as a single equity judge sitting here, say that these gentlemen when they bought this Saugerties mill in 1903 and spent their \$133,000, were not doing an act that was absolutely necessary to the preservation of the successful business of the corporation. There is direct evidence in the case which indicates that that was true. This energetic, capable manager, this expert, Mr. Thompson, the president, the head of this great enterprise, swears positively that they would have had to curtail their business, they could not have handled their or-

ders, without the acquisition of this mill or some other mill. Now, merely because they have nearly doubled the capital that they started out with in 1894 by constantly piling up their profits and adding them to their capital, I am not warranted in holding that dividends have unreasonably and unfairly been retained from distribution. The dividends distributed to the common stockholders, however, are exceedingly small. My recollection is that they averaged for five years less than four per cent. Beginning with 1890 during the years that have followed, this great business, in which such large gains have been made, has only yielded a little less than four per cent. to the holders of the stock. Well, it is perfectly plain that a court of equity cannot tolerate an indefinite continuation of that situation—the increasing of mills and machinery and vast expansion of this enterprise to the practical starvation of the stockholders. The situation would be very different, as counsel for the complainant very forcibly brought out in his argument and in his brief, if Mr. Raynolds' stock could be readily sold in the market and the market price of it increased as its book value increases, and these undistributed profits accumulate. If Mr. Raynolds held six hundred shares of stock in some of the banks or trust companies which have been established during the last ten years, it might make no difference to him whether dividends were paid from year to year or not. His share of these undistributed profits might be rendered to him completely from year to year in the shape of a steady increment of the market value of his stock. He might be able at any time and from time to time to realize such part of his share of the annual accumulation of profits as he might desire to have in the form of cash, by selling a few shares of his stock. But in fact in this case the complainant's stock is that of a private manufacturing corporation, a close corporation, whose stock does not appear to have any market value. There is nothing to suggest that Mr. Raynolds could have sold his stock, or any part of it, for any more money in 1904 than it would have brought in 1900. In the case of corporations of this class sales of stock outside of the small coterie of officers and managers are generally hard to make excepting upon disadvantageous terms. I think the distinction drawn by counsel for complainant between private manufacturing corporations like this paper mill company, and banks and trust companies, and even railroad companies, the shares of which are readily salable at all times on the market, and the market price of which is directly affected by the prosperity of the corporation, ought not to be overlooked in determining whether or not a dividend is being unreasonably and improperly withheld from expectant stockholders. In my opinion it is the plain duty of the majority of the stockholders of a corporation like this paper mill company, who also constitute its entire corps of salaried officers and managers, to bear in mind that the only sure benefit to the stockholders to be derived from the successful prosecution of the corporate business must come from the distribution

of dividends in cash, and that the piling up of a surplus which remains undistributed may in the end go wholly to future creditors of the corporation.

On the whole case, however, especially keeping in view the expenditure in 1903 of \$133,000 for the acquisition and equipment of the Saugerties mill, I do not think that a point was reached when this bill was filed at which it became the duty of this court to intervene and compel this corporation to declare a dividend for the benefit of its stockholders.

I think I have now stated the more important considerations which have led me to the conclusion that this court ought not now to set aside the judgment of these practical managers of such ability who are conducting their business apparently with great success and direct them to make a dividend, although, as I have heretofore intimated, an entirely different conclusion may be proper within a very short time.¹⁰

¹⁰ In *Stevens v. United States Steel Corporation* (1904) 68 N. J. Eq. 373, 59 Atl. 905, *Stevenson, V. C.* said: "The general rule is well settled that the directors of trading corporations are invested with a wide discretionary power in regard to the distribution of profits in the form of dividends among the stockholders. Subject, of course, to provisions in the charter, and also to the by-laws of the company, it is for the directors to say whether profits shall be distributed to the stockholders or retained for the purpose of the corporate business. It is, however, equally well settled that this discretionary power is not absolute, and when the directors 'improperly refuse to make a division of unused profits,' a court of equity will intervene on behalf of any stockholder who may complain."

See *Rollins v. Denver Club* (1908) 43 Colo. 345, 96 Pac. 188, 18 L. R. A. (N. S.) 733 (court loath to interfere); *Cratty v. Peoria Law Library Assn.* (1906) 219 Ill. 516, 76 N. E. 707 ("as to common stock, such discretion will not be interfered with by a court of equity in the absence of bad faith or arbitrary or unjustifiable conduct"); *Hunter v. Roberts* (1890) 83 Mich. 63, 47 N. W. 131; *Griffing v. Griffing Iron Co.* (1901) 61 N. J. Eq. 269, 48 Atl. 910; *Trimble v. American Sugar Refining Co.* (1901) 61 N. J. Eq. 340, 48 Atl. 912 (mere existence of "a large amount of surplus" not sufficient to warrant intervention); *McNab v. McNab & Harlin Mfg. Co.* (1891) 62 Hun (N. Y.) 18, 41 N. Y. St. 906, 16 N. Y. S. 448, *affd.* 133 N. Y. 687, 31 N. E. 627 (ultimate test is good faith); *Richardson v. Vermont &c. R. Co.* (1872) 44 Vt. 613; *Kaufman v. Charlottesville Woolen Mills Co.* (1896) 93 Va. 673, 25 S. E. 1003; *Morey v. Fish Bros. Wagon Co.* (1901) 108 Wis. 520, 84 N. W. 862; *Bernier v. Grescom-Spencer Co.* (1908) 161 Fed. 438; *N. Y. & R. v. Nickals* (1886) 119 U. S. 296, 7 Sup. Ct. 209, 30 L. ed. 363.

Cf. *Crichton v. Webb Press Co.* (1904) 113 La. 167, 36 So. 926, 67 L. R. A. 76, 101 Am. St. 500 (large surplus, dividend of \$50,000 declared); *Anderson v. W. J. Dyer & Bro.* (1904) 94 Minn. 30, 101 N. W. 1061 (fraud on minority shareholder); *Laurel Springs Land Co. v. Fougerey* (1893) 50 N. J. Eq. 756, 26 Atl. 886, reversing *Fougerey v. Cord* (1892) 50 N. J. Eq. 185 (fraudulent conduct of directors); *Scott v. Eagle Fire Co.* (1838) 7 Paige (N. Y.) 198, *esp. p.* 203.—Eds.

Section 4.—Right to Subscribe to New Stock.

CURRY v. SCOTT.

1867. 54 Pa. St. 270.¹

STRONG, J.—The objects sought to be attained by the bill are mainly such as are attainable by a writ of quo warranto, and it might perhaps be questioned whether they can be secured in a court of equity. A portion of the relief sought, however, is such as a court of law cannot give, and it is not assigned as one of the grounds of the demurrer that the plaintiff has an adequate remedy at law. We proceed, therefore, to inquire whether the bill exhibits a case entitling the plaintiff to relief.

It avers in substance that the Erie and Pittsburg Railroad Company, of which the plaintiff is a stockholder, having a portion of its authorized capital stock undisposed of, prescribed a time and manner for subscription of that which had previously remained untaken; that afterwards, and, so far as it appears, at the time and in the manner prescribed, John Van McCullom, one of the defendants, subscribed for all the stock that remained untaken, to wit, 7460 shares; that the company received his subscription, that he then paid on account of each share \$5; that the company issued certificates of stock for the stock thus taken; and that at the annual election next succeeding he was permitted to vote such shares. It is not averred that there was any fraud in the subscription or that the plaintiff or any other person was denied the privilege of subscribing or that the stock taken by McCullom was worth more than its par value at which he took it, but the bill rests upon the assumption that the directors of the company had no power thus to dispose of their untaken stock, and that McCullom could not thus acquire the rights of a stockholder to vote at an election.

The bill also avers that an Act of Assembly was passed on the 10th day of February, 1865, by which it was enacted that the board of directors of the Erie and Pittsburg Railroad Company be authorized to receive subscriptions for all or any part of the unsubscribed stock of said company under such regulations as to time and manner of such subscription as said directors should prescribe, any law or usage to the contrary notwithstanding, and that the subscribers to said stock should have the same rights in said company as if they had been original subscribers thereto. Provided, that any person subscribing therefor should pay at the time of subscribing \$5 on each share so subscribed. But the plaintiff insists that this act is of no force because it is an unwarranted infringement upon the rights of those who were stockholders at the time of its passage. And much of the argument has been expended

¹ The facts sufficiently appear in the opinion. Small portion of opinion omitted.—Eds.

in assailing and sustaining the validity of the enactment. We are of opinion, however, that the discussion was unnecessary, for without the act the directors of the company had power to receive subscriptions for all the untaken stock and issue certificates therefor. And the moment this was done the holder became a stockholder and entitled to the rights of a stockholder. The company was incorporated without any appointment of commissioners to receive subscriptions for stock, but it was enacted that the stock should consist of 20,000 shares of \$50 each. It was not required that any portion of it should be subscribed or paid in before the organization of the company, but the corporation was endowed at once with all the rights and privileges conferred by the General Railroad Act and its supplements. Of course subscriptions for stock were authorized after the organization until the authorized amount had been taken. And what else do new subscribers become than stockholders having equal rights with others? The law authorizes no distinction between the rights of one stockholder and those of another. If one has not paid his subscription in full he is a debtor for so much as remains unpaid, but he is none the less a shareholder.

It is insisted, however, that the directors had no right to allow McCullom to subscribe and thus obtain the untaken stock because it belonged to the old stockholders, and it should have been sold for their benefit, or they should have been allowed to take it in proportion to the shares they held. It would be a sufficient answer to this to say the bill does not allege that the plaintiff or any of the old stockholders offered or that they are willing to take it at par, nor does it allege that the stock could have been sold at a higher price than par. It therefore sets forth nothing that is injurious to the complainant. But when it is said that the untaken stock belonged to the old stockholders, more is meant than can be admitted. In a certain sense the assertion is true. But it is not to be admitted that an old stockholder had a right to subscribe to the untaken stock superior to the right of one who owned no stock. If this were so a first subscriber might compel all the remaining untaken stock to be sold, or, at least, would have a right to exclude any other person from subscribing.

The cases upon which the plaintiff relies are inapplicable to the case now in hand. In *Gray v. The Portland Bank*, 3 Mass. 364, it was held that when a banking company had been incorporated with a capital not less than one sum and not greater than another and had commenced business with the smaller capital, and afterwards voted to increase to the largest, those who held the stock in the capital first raised had a prior right to subscribe to the new stock. The case was really decided by two judges of a court consisting of five, but assuming its ruling to be sound law, it is unlike the case we have. Here is no increase of capital but a filling up of one both authorized and required. This is a substantial difference. So the case of *Reese v. The Bank of Montgomery County*, 7 Casey 78,

decides nothing more than that untaken stock is held by the corporation in trust for the corporators, and must be disposed of for the benefit of all; that it cannot be disposed of unequally to the corporators, and that if so disposed of, each corporator injured may have his action against the corporation. Neither of these cases decides that a stockholder has any greater right than a stranger to subscribe to original stock untaken. And we are unable to see why the directors of the Erie and Pittsburg Railroad could not permit McCullom to subscribe for all the untaken stock, why they could not issue certificates to him when he had subscribed, and why, having become thus a stockholder, he could not vote at an election. The Act of 1865 was then unnecessary, it was but a re-enactment of that which had been previously enacted. * * *

From what has been said it will be seen that, in our opinion, the plaintiff's bill exhibits no case calling upon a court of equity to grant him relief. The demurrer must, therefore, be sustained and the bill dismissed.²

STOKES v. CONTINENTAL TRUST CO.

1906. 186 N. Y. 285, 78 N. E. 1090.³

APPEAL from an order of the Appellate Division of the Supreme Court in the first judicial department, entered January 4, 1905, reversing a judgment in favor of plaintiff entered upon a decision of the court on trial at Special Term and granting a new trial.

This action was brought by a stockholder to compel his corporation to issue to him at par such a proportion of an increase made in its capital stock as the number of shares held by him before such increase bore to the number of all the shares originally issued, and in case such additional shares could not be delivered to him for his damages in the premises.

The defendant is a domestic banking corporation in the city of New York, organized in 1890, with a capital stock of \$500,000, consisting of 5,000 shares of the par value of \$100 each. The plaintiff was one of the original stockholders and still owns all the stock issued to him at the date of organization, together with enough more acquired since to make 221 shares in all. On the 29th of January, 1902, the defendant had a surplus of \$1,048,450.94 which made the book value of the stock at that time \$309.69 per share. On the 2nd of January, 1902, Blair & Company, a strong and influential firm of private bankers in the City of New York, made the following proposition to the defendant: "If your stockholders at the special meeting to be called for January 29th, 1902, vote to increase your capital stock from \$500,000 to \$1,000,000 you may

² State v. Smith (1876) 48 Vt. 266, *Accord*.

³ Portions of opinions omitted.—Eds.

deliver the additional stock to us as soon as issued at \$450 per share (\$100 par value) for ourselves and our associates, it being understood that we may nominate ten of the 21 trustees to be elected at the adjourned annual meeting of stockholders."

The directors of the defendant promptly met and duly authorized a special meeting of the stockholders to be called to meet on January 29th, 1902, for the purpose of voting upon the proposed increase of stock and the acceptance of the offer to purchase the same. Upon due notice a meeting of the stockholders was held accordingly, more than a majority attending either in person or by proxy. A resolution to increase the stock was adopted by the vote of 4,197 shares, all that were cast. Thereupon the plaintiff demanded from the defendant the right to subscribe for 221 shares of the new stock at par, and offered to pay immediately for the same, which demand was refused. A resolution directing a sale to Blair & Company at \$450 a share was then adopted by a vote of 3,596 shares to 241. The plaintiff voted for the first resolution but against the last, and before the adoption of the latter he protested against the proposed sale of his proportionate share of the stock and again demanded the right to subscribe and pay for the same, but the demand was refused.

On the 30th of January, 1902, the stock was increased, and on the same day was sold to Blair & Company at the price named. Although the plaintiff formally renewed his demand for 221 shares of the new stock at par and tendered payment therefor, it was refused upon the ground that the stock had already been issued to Blair & Company. Owing in part to the offer of Blair & Company, which had become known to the public, the market price of the stock had increased from \$450 a share in September, 1901, to \$550 in January, 1902, and at the time of the trial, in April, 1904, it was worth \$700 per share.

Prior to the special meeting of the stockholders, by authority of the board of directors a circular letter was sent to each stockholder, including the plaintiff, giving notice of the proposition made by Blair & Company and recommending that it be accepted. Thereupon the plaintiff notified the defendant that he wished to subscribe for his proportionate share of the new stock, if issued, and at no time did he waive his right to subscribe for the same. Before the special meeting, he had not been definitely notified by the defendant that he could not receive his proportionate part of the increase, but was informed that his proposition would "be taken under consideration."

After finding these facts in substance, the trial court found, as conclusions of law, that the plaintiff had the right to subscribe for such proportion of the increase, as his holdings bore to all the stock before the increase was made; that the stockholders, directors and officers of the defendant had no power to deprive him of that right, and that he was entitled to recover the difference between

the market value of 221 shares on the 30th of January, 1902, and the par value thereof, or the sum of \$99,450, together with interest from said date. The judgment entered accordingly was reversed by the Appellate Division, and the plaintiff appealed to this court, giving the usual stipulation for judgment absolute in case the order of reversal should be affirmed. * * *

VANN, J.—No exception worthy of notice appears in the record, except those filed to the conclusions of law found by the trial judge. If those conclusions are supported by the facts found, the Appellate Division had no power to reverse the judgment rendered by the Special Term on questions of law only, as, from the silence of the record, it must be presumed was done. (Code Civ. Pro. § 1338.) If the facts found did not warrant the legal conclusions of the trial court the order of reversal was right and should be affirmed. Thus the question presented for decision is whether according to the facts found the plaintiff had the legal right to subscribe for and take the same number of shares of the new stock that he held of the old? 7

The subject is not regulated by statute and the question presented has never been directly passed upon by this court, and only to a limited extent has it been considered by courts in this state. (Miller v. Illinois Central R. R. Co., 24 Barb. 312; Matter of Wheeler, 2 Abb. Pr. (N. S.) 361; Currie v. White, 45 N. Y. 822.)

In the first case cited judgment was rendered by a divided vote of the General Term in the first district. The court held that the plaintiff was entitled to no relief because he did not own any shares when the new stock was issued, but only an option, and that he could not claim to be an actual holder until he had exercised his right of election. The court further said, however, that if he was the owner of shares at the time of the new issue he had no absolute right as such owner to a distributive allotment of the new stock.

Matter of Wheeler was decided by Judge Mason at Special Term, and although the point was not directly involved, the learned judge said: "As I understand the law all these old stockholders had a right to share in the issuing of this new stock in proportion to the amount of stock held by them. And if none of the stock was to be apportioned to the old stockholders, they had certainly the right to have the new stock sold at public sale, and to the highest bidder, that they might share in the gains arising from the sale. In short, the old stockholders, as this was good stock and above par, had a property in the new stock, or a right at least to be secured the profits to be derived from a fair sale of it if they did not wish to purchase it themselves; and they have been deprived of this by the course which these directors have taken with this new stock by transferring or issuing it to themselves and others in a manner not authorized by law."

In Currie v. White the point was not directly involved, but Judge Folger, referring to the rights acquired under a certain contract,

said: "One of these rights was to take new shares upon any legitimate increase of the capital stock, which right attaches to the old shares, not as a profit or income, but as inherent in the shares in their very creation," citing *Atkins v. Albree* (12 Allen, 359); *Brander v. Brander* (4 Ves. 800, and notes, Sumner ed.). While this was said in a dissenting opinion, Judge Rapallo, who spoke for the court, concurred, saying, "As to the claim for the additional stock, I concur in the conclusions of my learned brother Folger." The fair implication from both opinions is that if the plaintiff had preserved his rights, he would have been entitled to the new stock.

In other jurisdictions the decisions support the claim of the plaintiff with the exception of *Ohio Insurance Co. v. Nunnemacher* (15 Ind. 294) which turned on the language of the charter. The leading authority is *Gray v. Portland Bank*, decided in 1807 and reported in 3 Mass. 364. In that case a verdict was found for the plaintiff, subject, by the agreement of the parties, to the opinion of the court upon the evidence in the case whether the plaintiff was entitled to recover, and, if so, as to the measure of damages. The court held that stockholders who held old stock had a right to subscribe for and take new stock in proportion to their respective shares. As the corporation refused this right to the plaintiff he was permitted to recover the excess of the market value above the par value, with interest. In the course of its argument the court said: "A share in the stock or trust when only the least sum has been paid in is a share in the power of increasing it when the trustee determines or rather when the cestuis que trustent agree upon employing a greater sum. * * * A vote to increase the capital stock, if it was not the creation of a new and disjointed capital, was in its nature an agreement among the stockholders to enlarge their shares in the amount or in the number to the extent required to effect that increase. * * * If from the progress of the institution and the expense incurred in it any advance upon the additional shares might be obtained in the market, this advance upon the shares relinquished belonged to the whole, and was not to be disposed of at the will of a majority of the stockholders to the partial benefit of some and exclusion of others."

This decision has stood unquestioned for nearly a hundred years and has been followed generally by courts of the highest standing. It is the foundation of the rule upon the subject that prevails, almost without exception, throughout the entire country.

In *Way v. American Grease Company* (60 N. J. Eq. 263, 269) the head note fairly expresses the decision as follows: "Directors of a corporation, which is fully organized and in the active conduct of its business, are bound to afford to existing stockholders an opportunity to subscribe for any new shares of its capital, in proportion to their holdings, before disposing of such new shares in any other way."

In *Eidman v. Bowman* (58 Ill. 444, 447) it was said: "When

this corporation was organized, the charter and all of its franchises and privileges vested in the shareholders and the directors became their trustees for its management. The right to the remainder of the stock, when it should be issued, vested in the original stockholders, in proportion to the amount each held of the original stock, if they would pay for it, and was as fully theirs as was the stock already held and for which they had paid."

In *Dousman v. Wisconsin, etc. Co.* (40 Wis. 418, 421) it was held that a court of equity would compel a corporation to issue to every stockholder his proportion of new stock on the ground that "he has a right to maintain his proportionate interest in the corporation, certainly as long as there is sufficient stock remaining undisposed of by the corporation."

In *Jones v. Morrison* (31 Minn. 140, 152) it was said: "When the proposition that a corporation is trustee of the corporate property for the benefit of the stockholders in proportion to the stock held by them is admitted (and we find no well considered case which denies it), it covers as well the power to issue new stock as any other franchise or property which may be of value, held by the corporation. The value of that power, where it has actual value, is given to it by the property acquired and the business built up with the money paid by the subsisting stockholders. It happens not infrequently that corporations, instead of distributing their profits in the way of dividends to stockholders, accumulate them till a large surplus is on hand. No one would deny that, in such case, each stockholder has an interest in the surplus which the courts will protect. No one would claim that the officers, directors or majority of the stockholders, without the consent of all, could give away the surplus, or devote it to any other than the general purposes of the corporation. But when new stock is issued, each share of it has an interest in the surplus equal to that pertaining to each share of the original stock. And if the corporation, either through the officers, directors or majority of the stockholders, may dispose of the new stock to whomsoever it will, at whatever price it may fix, then it has the power to diminish the value of each share of old stock by letting in other parties to an equal interest in the surplus and in the good will or value of the established business."

In *Real Estate Trust Co. v. Bird* (90 Md. 229, 245) the court said: "There can be no doubt that the general rule is that when the capital stock of a corporation is increased by the issue of new shares, authorized by the charter, the holders of the original stock are entitled to the new stock in the proportion that the number of shares held by them bears to the whole number before the increase."

In all these cases, as well as many others, *Gray v. Portland Bank* (supra) is followed without criticism or question. In some cases the same result is reached without citing that case. Thus in *Jones v. Concord & Montreal R. R. Co.* (67 N. H. 119) it was declared, as

stated in the head note, that "an issue of new shares of stock in an increase of the capital of a corporation is a partial division of the common property, which can be taken from the original shareholders only by their consent or by legal process."

So in *Bank of Montgomery v. Reese* (26 Pa. St. 143, 146; 31 id. 78) the court said: "Morgan L. Reese, as one of the stockholders of the Bank of Montgomery, was entitled to a portion of the unsold capital stock. His right was as valid as that of a tenant in common of real estate to his purpart on a partition. The corporation was a trustee for the stockholders, but in disregard of the duties of the trust in distributing this stock it deprived Mr. Reese of the number of shares to which he was entitled. He has established his right in this action." The question of power was broadly presented and decided.

In another case in the same state, *Morris v. Stevens* (178 Pa. St. 563, 578) Mr. Chief Justice Sterrett used the following language: "In general, the present holders of stock have a primary right to subscribe in proportion to their holdings for any new issue. The stockholders themselves certainly may determine otherwise and order a sale to the public and payment of the proceeds into the treasury. But this is exceptional and the exercise of a reserved power which should not be permitted unless there is a clear intent of the stockholders to do so." (See, also, *Cunningham's Appeal*, 108 Pa. St. 546; *Reading Trust Co. v. Reading Iron Works*, 137 Pa. St. 282; *De La Cuesta v. Ins. Co.*, 136 Pa. St. 62; *Humboldt Driving Park Assoc. v. Stevens*, 34 Neb. 528, 534; *Hart v. St. Charles Street R. R. Co.*, 30 La. Ann. 758; *State v. Smith*, 48 Vt. 290; *Atkins v. Albree*, 94 Mass. 359; *Hammond v. Edison Illuminating Co.*, 131 Mich. 79; *Knapp v. Publishers George Knapp & Co.*, 127 Mo. 53; *Baltimore City Pass. R. Co. v. Hambleton*, 77 Md. 341; *Jones v. C. & M. R. R. Co.*, 67 N. H. 119; *Id.* 234.)

The elementary writers are very clear and emphatic in laying down the same rule. (The learned judge here referred to 2 *Beach on Private Corporations*, Sec. 473; 1 *Cook on Corporations* (4th ed.) 286; 10 *Cyc.* 543; 26 *Am. & Eng. Encyc.* (2d ed.) 947; 2 *Thompson's Commentaries*, Sec. 2094; *Angell & Ames on Corporations*, 430; *Morawetz on Corporations*, Sec. 455.)

If the right claimed by the plaintiff was a right of property belonging to him as a stockholder he could not be deprived of it by the joint action of the other stockholders and of all the directors and officers of the corporation.

What is the nature of the right acquired by a stockholder through the ownership of shares of stock? What rights can he assert against the will of a majority of the stockholders and all the officers and directors? While he does not own and cannot dispose of any specific property of the corporation, yet he and his associates own the corporation itself, its charter, franchises and all rights conferred thereby, including the right to increase the stock. He has an

inherent right to his proportionate share of any dividend declared, or of any surplus arising upon dissolution, and he can prevent waste or misappropriation of the property of the corporation by those in control. Finally, he has the right to vote for directors and upon all propositions subject by law to the control of the stockholders, and this is his supreme right and main protection. Stockholders have no direct voice in transacting the corporate business, but through their right to vote they can select those to whom the law intrusts the power of management and control.

A corporation is somewhat like a partnership, if one were possible, conducted wholly by agents where the copartners have power to appoint the agents, but are not responsible for their acts. The power to manage its affairs resides in the directors, who are its agents, but the power to elect directors resides in the stockholders. This right to vote for directors and upon propositions to increase the stock or mortgage the assets, is about all the power the stockholder has. So long as the management is honest, within the corporate powers and involves no waste, the stockholders cannot interfere, even if the administration is feeble and unsatisfactory, but must correct such evils through their power to elect other directors. Hence, the power of the individual stockholder to vote in proportion to the number of his shares, is vital and cannot be cut off or curtailed by the action of all the other stockholders even with the cooperation of the directors and officers.

In the case before us the new stock came into existence through the exercise of a right belonging wholly to the stockholders. As the right to increase the stock belonged to them, the stock when increased belonged to them also, as it was issued for money and not for property or for some purpose other than the sale thereof for money. By the increase of stock the voting power of the plaintiff was reduced one-half, and while he consented to the increase he did not consent to the disposition of the new stock by a sale thereof to Blair & Company at less than its market value, nor by sale to any person in any way except by an allotment to the stockholders. The increase and sale involved the transfer of rights belonging to the stockholders as part of their investment. The issue of new stock and the sale thereof to Blair & Company was not only a transfer to them of one-half the voting power of the old stockholders, but also of an equitable right to one-half the surplus which belonged to them. In other words, it was a partial division of the property of the old stockholders. The right to increase stock is not an asset of the corporation any more than the original stock when it was issued pursuant to subscription. The ownership of stock is in the nature of an inherent but indirect power to control the corporation. The stock when issued ready for delivery does not belong to the corporation in the way that it holds its real and personal property, with power to sell the same, but is held by it with no power of alienation in trust for the stockholders, who are the beneficial owners and become the legal owners upon paying

therefor. The corporation has no rights hostile to those of the stockholders, but is the trustee for all including the minority. The new stock issued by the defendant under the permission of the statute did not belong to it, but was held by it the same as the original stock when first issued was held in trust for the stockholders. It has the same voting power as the old, share for share. The stockholders decided to enlarge their holdings, not by increasing the amount of each share, but by increasing the number of shares. The new stock belonged to the stockholders as an inherent right by virtue of their being stockholders, to be shared in proportion upon paying its par value or the value per share fixed by vote of a majority of the stockholders, or ascertained by a sale at public auction. While the corporation could not compel the plaintiff to take new shares at any price, since they were issued for money and not for property, it could not lawfully dispose of those shares without giving him a chance to get his proportion at the same price that outsiders got theirs. He had an inchoate right to one share of the new stock for each share owned by him of the old stock, provided he was ready to pay the price fixed by the stockholders. If so situated that he could not take it himself, he was entitled to sell the right to one who could, as is frequently done. Even this gives an advantage to capital, but capital necessarily has some advantage. Of course, there is a distinction when the new stock is issued in payment for property, but that is not this case. The stock in question was issued to be sold for money and was sold for money only. A majority of the stockholders, as part of their power to increase the stock, may attach reasonable conditions to the disposition thereof, such as the requirement that every old stockholder electing to take new stock shall pay a fixed price therefor, not less than par, however, owing to the limitation of the statute. They may also provide for a sale in parcels or bulk at public auction, when every stockholder can bid the same as strangers. They cannot, however, dispose of it to strangers against the protest of any stockholder who insists that he has a right to his proportion. Otherwise the majority could deprive the minority of their proportionate power in the election of directors and of their proportionate right to share in the surplus, each of which is an inherent, pre-emptive and vested right of property. It is inviolable and can neither be taken away nor lessened without consent, or a waiver implying consent. The plaintiff had power, before the increase of stock, to vote on 221 shares of stock, out of a total of 5,000, at any meeting held by the stockholders for any purpose. By the action of the majority, taken against his will and protest, he now has only one-half the voting power that he had before, because the number of shares has been doubled while he still owns but 221. This touches him as a stockholder in such a way as to deprive him of a right of property. Blair & Company acquired virtual control, while he and the other stockholders lost it. We are not discussing equities, but legal rights, for this is an action at law, and the plaintiff was deprived of a strictly legal right. If the result

gives him an advantage over other stockholders, it is because he stood upon his legal rights, while they did not. The question is what were his legal rights, not what his profits may be under the sale to Blair & Company, but what it might have been if the new stock had been issued to him in proportion to his holding of the old. The other stockholders could give their property to Blair & Company, but they could not give his.

A share of stock is a share in the power to increase the stock, and belongs to the stockholders the same as the stock itself. When that power is exercised, the new stock belongs to the old stockholders in proportion to their holding of old stock, subject to compliance with the lawful terms upon which it is issued. When the new stock is issued in payment for property purchased by the corporation, the stockholders' right is merged in the purchase, and they have an advantage in the increase of the property of the corporation in proportion to the increase of stock. When the new stock is issued for money, while the stockholders may provide that it be sold at auction or fix the price at which it is to be sold, each stockholder is entitled to his proportion of the proceeds of the sale at auction, after he has had a right to bid at the sale, or to his proportion of the new stock at the price fixed by the stockholders.

We are thus led to lay down the rule that a stockholder has an inherent right to a proportionate share of new stock issued for money only and not to purchase property for the purposes of the corporation or to effect a consolidation, and while he can waive that right, he cannot be deprived of it without his consent except when the stock is issued at a fixed price not less than par and he is given the right to take at that price in proportion to his holding, or in some other equitable way that will enable him to protect his interest by acting on his own judgment and using his own resources. This rule is just to all and tends to prevent the tyranny of majorities which needs restraint, as well as virtual attempts to blackmail by small minorities which should be prevented.

The remaining question is whether the plaintiff waived his rights by failing to do what he ought to have done, or by doing something he ought not to have done. He demanded his share of the new stock at par, instead of at the price fixed by the stockholders, for the authorization to sell at \$450 a share was virtually fixing the price of the stock. He did more than this, however, for he not only voted against the proposition to sell to Blair & Company at \$450, but as the court expressly found, he "protested against the proposed sale of his proportionate share of the stock and again demanded the right to subscribe and pay for the same which demands were again refused," and "the resolution was carried notwithstanding such protest and demands." Thus he protested against the sale of his share before the price was fixed, for the same resolution fixed the price and directed the sale, which was promptly carried into effect. If he had not attended the meeting, called upon due notice to do pre-

cisely what was done, perhaps he would have waived his rights, but he attended the meeting and before the price was fixed demanded the right to subscribe for 221 shares at par and offered to pay for the same immediately. It is true that after the price was fixed he did not offer to take his share at that price, but he did not acquiesce in the sale of his proportion to Blair & Company, and unless he acquiesced the sale as to him was without right. He was under no obligation to put the corporation in default by making a demand. The ordinary doctrine of demand, tender and refusal has no application to this case. The plaintiff had made no contract. He had not promised to do anything. No duty of performance rested upon him. He had an absolute right to the new stock in proportion to his holding of the old and he gave notice that he wanted it. It was his property and could not be disposed of without his consent. He did not consent. He protested in due time, and the sale was made in defiance of his protest. While in connection with his protest he demanded the right to subscribe at par, that demand was entirely proper when made, because the price had not then been fixed. After the price was fixed it was the duty of the defendant to offer him his proportion at that price, for it had notice that he had not acquiesced in the proposed sale of his share, but wanted it himself. The directors were under the legal obligation to give him an opportunity to purchase at the price fixed before they could sell his property to a third party, even with the approval of a large majority of the stockholders. If he had remained silent and had made no request or protest he would have waived his rights, but after he had given notice that he wanted his part and had protested against the sale thereof, the defendant was bound to offer it to him at the price fixed by the stockholders. By selling to strangers without thus offering to sell to him, the defendant wrongfully deprived him of his property and is liable for such damages as he actually sustained.

The learned trial court, however, did not measure the damages according to law. The plaintiff was not entitled to the difference between the par value of the new stock and the market value thereof, for the stockholders had the right to fix the price at which the stock should be sold. They fixed the price at \$450 a share, and for the failure of the defendant to offer the plaintiff his share at that price we hold it liable in damages. His actual loss, therefore, is \$100 per share, or the difference between \$450, the price that he would have been obliged to pay had he been permitted to purchase, and the market value on the day of sale, which was \$550. This conclusion requires a reversal of the judgment rendered by the Appellate Division and a modification of that rendered by the trial court.

The order appealed from should be reversed and the judgment of the trial court modified by reducing the damages from the sum of \$99,450, with interest from January 30th, 1902, to the sum of \$22,100, with interest from that date, and by striking out the extra allowance of costs, and as thus modified the judgment of the trial court is

affirmed, without costs in this court or in the Appellate Division to either party.

HAIGHT, J. (dissenting).—I agree that the rule that we should adopt is that a stockholder in a corporation has an inherent right to purchase a proportionate share of new stock issued for money only, and not to purchase property necessary for the purposes of the corporation or to effect a consolidation. While he can waive that right he cannot be deprived of it without his consent, except by sale at a fixed price at or above par, in which he may buy at that price in proportion to his holding or in some other equitable way that will enable him to protect his interest by acting on his own judgment and using his own resources. I, however, differ with Judge Vann as to his conclusions as to the rights of the plaintiff herein. Under the findings of the trial court the plaintiff demanded that his share of the new stock should be issued to him at par, or \$100 per share, instead of \$450 per share, the price offered by Blair & Company and the price fixed at the stockholders' meeting at which the new stock was authorized to be sold. This demand was made after the passage of the resolution authorizing the increase of the capital stock of the defendant company and before the passage of the resolution authorizing a sale of the new stock to Blair & Company at the price specified. After the passage of the second resolution he objected to the sale of his proportionate share of the new stock to Blair & Company and again demanded that it be issued to him, and the following day he made a legal tender for the amount of his portion of the new stock at \$100 per share. There is no finding of fact or evidence in the record showing that he was ever ready or willing to pay \$450 per share for the stock. He knew that Blair & Company represented Marshall Field and others at Chicago, great dry goods merchants, and that they had made a written offer to purchase the new stock of the company provided the stockholders would authorize an increase of its capital stock from five hundred thousand to a million dollars. He knew that the trustees of the company had called a special meeting of the stockholders for the purpose of considering the offer so made by Blair & Company. He knew that the increased capitalization proposed was for the purpose of enlarging the business of the company and bringing into its management the gentlemen referred to. There is no pretense that any of the stockholders would have voted for an increase of the capital stock otherwise than for the purpose of accepting the offer of Blair & Company. All were evidently desirous of interesting the gentlemen referred to in the company, and by securing their business and deposits increase the earnings of the company. This the trustees carefully considered, and in their notice calling the special meeting of the stockholders distinctly recommended the acceptance of the offer. What, then, was the legal effect of the plaintiff's demand and tender? To my mind it was simply an attempt to make something out of his associates, to get for \$100 per

share the stock which Blair & Company had offered to purchase for \$450 per share; and that it was the equivalent of a refusal to pay \$450 per share, and its effect is to waive his right to procure the stock by paying that amount. An acceptance of his offer would have been most unjust to the remaining stockholders. It would not only have deprived them of the additional sum of \$350 per share, which had been offered for the stock, but it would have defeated the object and purpose for which the meeting was called, for it was well understood that Blair & Company would not accept less than the whole issue of the new stock. But this is not all. It appears that prior to the offer of Blair & Company the stock of the company had never been sold above \$450 per share; that thereafter the stock rapidly advanced until the day of the completion of the sale on the 30th of January, when its market value was \$550 per share; but this, under the stipulation of facts, was caused by the rumor and subsequent announcement and consummation of the proposition for the increase of the stock and the sale of such increase to Blair & Company and their associates. It is now proposed to give the plaintiff as damages such increase in the market value of the stock, even though such value was based upon the understanding that Blair & Company were to become stockholders in the corporation, which the acceptance of plaintiff's offer would have prevented. This, to my mind, should not be done. I, therefore, favor an affirmance.

Cullen, Ch. J., Werner and Hiscock, JJ., concur with Vann, J.; Willard Bartlett, J., concurs with Haight, J.; O'Brien, J., absent.
*Ordered accordingly.*⁴

Section 5.—Right to Inspection of Corporate Books and Records.

VARNEY v. BAKER.

1906. 194 Mass. 239, 80 N. E. 524.

KNOWLTON, C. J.—This is a petition for a writ of mandamus to obtain an examination of the books of account of the defendant corporation.* The petitioner is the owner of eighty shares of the capital stock of the corporation, the whole number of shares being three hundred and fifty. The respondent Baker admitted that he told the son of the petitioner, three or four months before the petition was filed, that the company had lost several thousand dollars. The truth of the statement was not denied, although officers of the

⁴ See note to principal case in 12 L. R. A. (N. S.) 969, and *cf.* *Hammond v. Edison Illuminating Co.* (1902) 131 Mich. 79, 90 N. W. 1040, 100 Am. St. 582. See also *Russell v. American Gas & Elec. Co.* (1912) 136 N. Y. S. 602, and notes, 26 Harv. L. Rev. 75, 13 Columbia L. Rev. 146, as to preferred shareholder's right of preemption.—Eds.

* The Baker Shoe Company, a corporation organized under the general laws of Massachusetts.

company testified that at the time of the hearing, the company was in a prosperous condition.

The single justice who heard the case found that the petitioner honestly believes that the company is being mismanaged, and desires in good faith, for the protection of his interest in the corporation, to examine the books and records of the company for the purpose of ascertaining its condition and the value of its stock, and of determining what to do with his stock, and whether there has been mismanagement of the corporation, and if so, what effect it has had upon the assets and business of the corporation, in order that he may be enabled to bring a bill in equity for the appointment of a receiver, or to take other proper proceedings for the benefit of the corporation and of his interest therein. He also found that an examination could be conducted without interfering unduly with the business of the corporation. It was not proved to the satisfaction of the justice that there was any mismanagement in fact, or any incapacity on the part of the managing officers. The justice reserved the case for our determination, and his report presents the question of law whether, on these facts, the petitioner should have an opportunity to examine the books of account and deposit of the corporation, and if so, to what extent.

The stockholders of a corporation are the equitable owners of its assets, and the officers act in a fiduciary relation as agents of the corporation and of the stockholders. They should be ready to account to the stockholders for their doings at all reasonable times, and the stockholders have a right to inspect their records and accounts, and to ascertain whether they are faithful, honest and intelligent in the performance of their duties. There is no good reason why the stockholders, acting in good faith for the purpose of advancing the interest of the corporation and protecting their rights as owners, should not be permitted to examine the corporate property, including the books and accounts.

It was formerly held in England that this right could be exercised, against the will of the managing officers, only when there was a specific dispute about some corporate matter, between the stockholders and the officers. *Rex v. Merchant Tailors' Co.* 2 B. & Ad. 115. But this rule has been modified by statute. See St. 8 & 9 Vict. c. 16, Secs. 117, 119, and St. 25 & 26 Vict. c. 89, Table A 78. The doctrine has not been adopted in America, the cases which go furthest in that direction holding that a dispute as to the alleged mismanagement of the corporation is enough to entitle the stockholder to an examination of the accounts to see whether there is a ground for an action. *Commonwealth v. Phoenix Iron Co.*, 105 Penn. St. 111. *Phoenix Iron Co. v. Commonwealth*, 113 Penn. St. 563. According to the general rule in this country, it is not necessary that there should be any particular dispute to entitle the stockholder to exercise this right. Nothing more is required than that, acting in good faith for the protection of the interests of the cor-

poration and his own interests, he desires to ascertain the condition of the company's business. *Guthrie v. Harkness*, 199 U. S. 148. *In re Steinway*, 159 N. Y. 250. *Huyler v. Cragin Cattle Co.* 13 Stew. (N. J.) 392. *State v. Pacific Brewing & Malting Co.* 21 Wash. 451. *Cockburn v. Union Bank of Louisiana*, 13 La. Ann. 289. *State v. Laughlin*, 53 Mo. App. 542. *Heminway v. Heminway*, 58 Conn. 443. See *Union Bank v. Knapp*, 3 Pick. 96, 108.

Of course the right at common law is not absolute, so that it can be exercised for mere curiosity, or for merely speculative purposes, or vexatiously. (If the court is appealed to for the enforcement of the right, a sound discretion will be exercised to determine whether the petitioner is acting for an honest purpose, not adverse to the interests of the corporation.) The court will consider whether his desire for an examination is reasonable, having reference to the interests of the corporation and his personal interest as a member of it. Its effect upon the corporation in reference to competitors and other interests will not be disregarded. But as was stated in *Dunphy v. Traveller Newspaper Association*, 146 Mass. 495, "Courts of equity are swift to protect helpless minorities of stockholders of corporations from the oppression and fraud of majorities."

In the present case the findings of the justice show that the petitioner should be permitted to examine the books in accordance with his request. His right to such an examination includes the right to have the assistance of an expert, or other person, if he desires to make transcripts from the books for subsequent use.

There is nothing in our statutes which enlarges or diminishes this right as it exists at common law. The provision of the St. 1903, c. 437, Sec. 30, relates only to the copies, books and records therein referred to, and is not applicable to the present case.

*Peremptory writ of mandamus to issue.*¹

VENNER v. CHICAGO CITY RAILWAY CO.

1910. 246 Illinois 170, 92 N. E. 643.²

APPEAL from the Appellate Court for the First District;—heard in that court on appeal from the Superior Court of Cook County; the Hon. Ben M. Smith, Judge, presiding.

¹*In re Steinway* (1899) 159 N. Y. 250, 53 N. E. 1103, 45 L. R. A. 461n, *Accord*.

"It does not follow that the courts will compel the inspection of the bank's books under all circumstances. In issuing the writ of mandamus the court will exercise a sound discretion and grant the right under proper safeguards to protect the interests of all concerned. The writ should not be granted for speculative purposes or to gratify idle curiosity or to aid a blackmailer, but it may not be denied to the stockholder who seeks the information for legitimate purposes." *Per* Mr. Justice Day in *Guthrie v. Harkness* (1905) 199 U. S. 148, at p. 156, 26 Sup. Ct. 4, 50 L. ed. 130.—Eds.

²Portion of opinion and dissenting opinions of Carter, J. and Cartwright, J. omitted.—Eds.

Mr. CHIEF JUSTICE VICKERS delivered the opinion of the court: Clarence H. Venner filed a petition for mandamus against the Chicago City Railway Company and its president and secretary to compel the defendants to permit him to examine the books, records and accounts of the company which were under the control of the president and secretary thereof. A demurrer having been sustained to the petition an amended petition was filed, alleging that Venner acquired certain shares of stock of the Chicago City Railway Company in the year 1905, which he held at the time the petition was filed. He alleged that he had made frequent applications to the company for the privilege of examining its books and that he had been denied such right. The amended petition contains other averments which were intended to support the application for mandamus on common law grounds. In the view that we have of this controversy it will not be necessary to determine the sufficiency of the petition under the common law, and therefore not necessary to set out those averments in the petition. A demurrer interposed to the answer filed by defendants was carried back and sustained to the amended petition. The petitioner elected to abide by his amended petition, and it was dismissed and judgment rendered against petitioner for costs. The Appellate Court for the First District affirmed the judgment below, and the cause has been brought to this court by petitioner on a certificate of importance.

Section 13 of chapter 32 of Hurd's Revised Statutes of 1909 provides as follows: "It shall be the duty of the directors or trustees of every stock corporation to cause to be kept at its principal office or place of business in this State, correct books of account of all its business, and every stockholder in such corporation shall have the right at all reasonable times, by himself or by his attorney, to examine the records and books of account of the corporation." This section of the statute is a part of our general act concerning corporations for pecuniary profit, which was approved April 18, 1872, and went into force July 1, 1872.

The Chicago City Railway Company was incorporated under a special public act of the legislature, which was approved February 14, 1859, and by its terms went into force from and after its passage. The act of 1859 created certain persons therein named a body corporate, by the name of "The Chicago City Railway Company," and authorized the said corporation to "construct, maintain and operate a single or double track railway, with all necessary and convenient tracks for turn-outs, side-tracks and appendages, in the city of Chicago, and in, on, over and along said street or streets, highway or highways, bridge or bridges, river or rivers, within the present or future limits of the south or west division of the city of Chicago, as the said council of said city have authorized said corporators or any of them, or shall authorize said corporators so to

do." The capital stock of the said corporation was fixed at \$100,000, with power to increase from time to time at the pleasure of said corporation, and it was provided by section 4 of said act that "all the corporate powers of said corporation shall be vested in and exercised by a board of directors and such officers and agents as said board shall appoint. * * * They [the board of directors] may also adopt such by-laws, rules and regulations for the government of said corporation and the management of its affairs and business as they may think proper, not inconsistent with the laws of this State."

There is nothing in the act of 1859 in relation to the keeping of books by the corporation or the inspection thereof by the stockholders, and no express declaration in said act that the corporation thereby chartered should be subject to laws that might thereafter be passed by the legislature. Under the situation thus presented appellant contends that he has a statutory right, under section 13 of the general Corporation act, to inspect the books of the company. Appellees deny that the Chicago City Railway Company is subject to section 13, and insist that appellant's right to the inspection of its books exists only under the common law and must be exercised in accordance therewith.

There is a well recognized distinction between the right of a stockholder to inspect the books and papers of a corporation under the common law and an unlimited right given by statute. Under the former the examination can only be compelled where the stockholder asks it in good faith and for reasons connected with his rights as a stockholder. (Heminway v. Heminway, 58 Conn. 443; Sage v. Lake Shore Railroad Co. 70 N. Y. 220; Phoenix Iron Co. v. Commonwealth, 113 Pa. St. 563; Stone v. Kellogg, 165 Ill. 192.) Where the right is conferred by statute in absolute terms, the purpose or motive of the stockholder in making the demand for an inspection is not material and he cannot be required to state his reasons therefor. (Thompson on Corporations,—2d ed.—sec. 4516.) The weight of American authority is to the effect that where the right is statutory the stockholder need not aver or show the object of his inspection, and it is no defense under a statute granting the absolute right to inspection to allege improper purposes or that the petitioner desires the information for the purpose of injuring the business of the corporation. A clear legal right given by a statute cannot be defeated by showing an improper motive. If this were so, the stockholder would be driven from a certain definite right given him by the statute, to the realm of uncertainty and speculation. (Thompson on Corporations, supra; Johnson v. Langdon, 135 Cal. 624; 87 Am. St. Rep. 156.) Leaving out of view entirely the sufficiency of the petition under the common law it must be conceded that it is sufficient under the statute, and it follows that if section 13 of the general Corporation law applies to the Chicago City Railway Company, the court erred in sustaining the demurrer to and dismissing the amended petition. * * *

(The learned judge *held* that section 13 of the general Corporation law did apply to the Chicago City Railway Company.)

From what has been said it follows that the court erred in sustaining the demurrer to the petition.

The judgments of the Appellate and Superior courts are reversed and the cause is remanded to the superior court for further proceedings in accordance with the views herein expressed.¹

*Reversed and remanded.*²

¹ Cf. *Stone v. Kellogg* (1897) 165 Ill. 192, 46 N. E. 222, 56 Am. St. 240. *Contra*, *Peo. ex rel. Britton v. Amer. Press Assn.* (1912) 148 App. Div. (N. Y.) 651, 133 N. Y. S. 216 (two justices dissenting), and notes, 12 Columbia Law Rev. 274, 25 Harv. Law Rev. 662.

See *Mutter v. Eastern & C. R. Co.* (1888) L. R. 38 Ch. Div. 92.—Eds.

Section 6.—Preferred Stock.**ANDREWS v. GAS METER CO.**1897. L. R. (1897) 1 Ch. Div. 361.¹

This action was brought by the holder of thirty ordinary shares against the defendant Finlay, the holder of 160 preference shares, and the company, claiming on behalf of plaintiff and the other ordinary shareholders: (1) A declaration that all profits of the defendant company, after providing for the preferential dividend belonged to the common shareholders; (2) to have it determined how and in what proportion the profits of the company, after providing for the preferential dividend, ought to be divided between the ordinary and preference shareholders.

The remaining facts sufficiently appear from the opinion.

LINDLEY L. J. delivered the judgment of the Court (Lindley, A. L. Smith, and Rigby L.JJ.) as follows:—The question raised by this appeal is whether certain preference shares issued by a limited company as long ago as 1865 were validly issued or not. If they were not, a further question will arise, which is—what are the rights of their present holders? The company was formed and registered as a limited company under the Companies Act, 1856; but in October, 1862, it was registered under the Companies Act, 1862, and it is by that Act and the decisions upon it that the above questions have to be determined. The company's original capital as stated in its memorandum of association was "60,000 *l.*, divided into 600 shares of 100 *l.* each, every share being sub-divisible into fifths, with power to increase the capital as provided by the articles of association." By the articles of association which accompanied the memorandum of association, and were registered with it, power was given to the company to increase the capital (art. 27), and it was provided that any new capital should be considered as part of the original capital (art. 28). The issue of preference shares was not contemplated or authorized. In 1865 the company desired to acquire additional works, and passed a special resolution under the powers conferred by the Companies Act, 1862, ss. 50 and 51, altering the articles and authorizing the issue of 100 shares of 100 *l.* each, fully paid, and bearing a preferential dividend of 5 *l.* per cent. per annum. Those shares were accordingly issued to the vendors of the works referred to, and are the shares the validity of which is now in question. The company has been prosperous, and the ordinary shareholders have for years received a higher dividend than the preference shareholders. A considerable reserve has also been accumulated, and this action has been brought to determine the rights of the preference shareholders to this reserve fund. The learned judge has held that the creation of preference shares was *ultra vires*, and that

¹ Statement rewritten. Concurring opinion of Rigby, L. J., omitted.—Eds.

their holders never became and are not now shareholders in the company, and that they have none of the rights of shareholders, whether preference or ordinary. He has not, however, declared more definitely what their rights are. They have appealed from this decision; but on the appeal they only claimed to be preference shareholders entitled to a preferential dividend of 5 per cent. Their claim to any share of the reserve fund was dropped. The judgment against the validity of the preference shares is based upon the well-known case of *Hutton v. Scarborough Cliff Hotel Co.* (1), which came twice before *Kindersley V.-C.* in 1865, and which *Kekewich J.* very naturally held to be binding on him. *Kindersley V.-C.*'s first decision was that a limited company which had not issued the whole of its original capital could not issue the unallotted shares as preference shares unless authorized so to do by its memorandum of association or by its articles of association. This decision was affirmed on appeal (2), and was obviously correct; and would have been correct even if the whole of the original capital had been issued and the preference shares had been new and additional capital. The company, however, afterward passed a special resolution altering the articles and authorizing an issue of preference shares. This raised an entirely different question, and led to the second decision. (3) The Vice-Chancellor granted an injunction restraining the issue of the preference shares, and he held distinctly that the resolution altering the articles was *ultra vires*. He did so upon the ground, as we understand his judgment, that there was in the memorandum of association a condition that all the shareholders should stand on an equal footing as to the receipt of dividends, and that this condition was one which could not be got rid of by a special resolution altering the articles of association under the powers conferred by ss. 50 and 51 of the Act. The judgment of the Vice-Chancellor is a little obscure, because he treats the condition as a condition of the constitution of the company, and he may have meant by that expression either the constitution as fixed by the memorandum of association or the constitution as fixed by the memorandum of association and the original articles. But unless he had meant the constitution of the company as fixed by the memorandum of association his decision is unintelligible; for, so far as the constitution depended on the articles, it clearly could be altered by special resolution under the powers conferred by ss. 50 and 51 of the Act. A company cannot deprive itself of this power: see *Malleson v. National Insurance and Guarantee Corporation* (4) and *Walker v. London Tramways Co.* (5) The Vice-Chancellor further seems to have been of the opinion that the condition could be excluded by contemporaneous articles of association, and his decision has been so understood by succeeding

(1) 2 Dr. & Sm. 514, 521.

(2) 4 D. J. & S. 672.

(3) 2 Dr. & Sm. 521.

(4) [1894] 1 Ch. 200.

(5) (1879) 12 Ch. D. 705.

judges. Accordingly, in 1875, in the case of *Harrison v. Mexican Ry. Co.* (6), Sir G. Jessel held that the condition of equality imported into the memorandum of association by *Kindersley V.-C.*'s decision was negatived by one of the articles of association filed with the memorandum, and which article authorized the creation of additional capital by the issue of new shares, "in such manner, to such amount, and with and subject to such rules, regulations, privileges, and conditions, as the company should think fit. In our opinion it is impossible to uphold this decision, or the view of *Kindersley V.-C.* himself, as to the effect of articles on the memorandum, if it is once conceded that it is a condition in the memorandum of association that there shall be equality amongst the shareholders. If the condition is really one of the conditions of the memorandum, it is immaterial whether the condition is express or implied. If the memorandum of association really prescribed equality amongst all the shareholders, as *Kindersley V.-C.* held that it did, the articles of association could not override the memorandum of association in that particular. See s. 12 of the Act, and *Ashbury Railway Carriage and Iron Co. v. Riche* (1) and *Guinness v. Land Corporation of Ireland*. (2) The departure thus made by Sir G. Jessel from the principle on which the Vice-Chancellor based the second decision in *Hutton v. Scarborough Cliff Hotel Co.* (3) was sanctioned by the Court of Appeal in 1885 in the case of *In re South Durham Brewery Co.* (4), and again in 1888 in *In re Bridge-water Navigation Co.* (5), a case which, although reversed on another point (6), was not questioned on the point now under consideration. These decisions turned upon the principle that although by s. 8 of the Act the memorandum is to state the amount of the original capital and the number of shares into which it is to be divided, yet in other respects the rights of the shareholders in respect of their shares and the terms on which additional capital may be raised are matters to be regulated by the articles of association rather than by the memorandum, and are, therefore, matters which (unless provided for by the memorandum, as in *Ashbury v. Watson* (7) may be determined by the company from time to time by special resolution pursuant to s. 50 of the Act. This view, however, clearly negatives the doctrine that there is a condition in the memorandum of association that all shareholders are to be on an equality unless the memorandum itself shews the contrary. That proposition is, in our opinion, unsound. Its unsoundness was distinctly pointed out by Lord Macnaghten in *British and American Trustee*

(6) L. R. 19 Eq. 358.

(1) (1875) L. R. 7 H. L. 653, 667.

(2) 22 Ch. D. 349.

(3) 2 Dr. & Sm. 521.

(4) 31 Ch. D. 261.

(5) 39 Ch. D. 1.

(6) (1889) 14 App. Cas. 525.

(7) 30 Ch. D. 376.

and Finance Corporation v. Couper. (8) The view taken by Kindersley V.-C. cannot, in our opinion, be supported by reference to the Companies Act of 1862; and it is inconsistent with the decisions to which we have referred, and which, if wrong, can only now be set right by the House of Lords.

It was, however, contended that this Court, at all events, had approved and followed the decision of Kindersley V.-C.; and Ashbury v. Watson (1) was referred to on this point. In that case the memorandum of association stated that preferential shares might be created, and what the preferential rights were to be; and it was held that these were conditions which could be properly introduced into the memorandum of association, and which, being introduced there, could not be afterwards departed from and be treated as articles of association capable of change. No doubt Fry L. J. relied on Hutton v. Scarborough Cliff Hotel Co. (2) to shew that provisions about preference shares were conditions which could properly be inserted in the memorandum of association; but the propriety of the decision of Kindersley V.-C. in that case was not before the Court, and we do not regard Ashbury v. Watson as conflicting with any of the other decisions of the Court of Appeal, in which Kindersley V.-C.'s decision has been judicially considered.

We desire to add that we do not base our judgment in this case on the words "with power to increase the capital as provided by the articles of association," which are in the memorandum of association. That power would have existed under s. 12 of the Act if those words had not been in the memorandum. We prefer to rest our decision on the grounds above explained. But the words in the memorandum to which we are now referring certainly shew that the conditions on which new capital was to be issued were not to be implied from the memorandum of association, but were to be ascertained from the articles; and as these might be changed from time to time under the powers conferred by ss. 50 and 51 of the Companies Act, 1862, it would follow from Harrison v. Mexican Ry. Co. (3), and other cases like it, that the resolutions of 1865 would be valid, even if the second decision could still be regarded as good law.

For the reasons, however, which we have given we are of opinion that the second decision in Hutton v. Scarborough Cliff Hotel Co. (2) was wrong, and ought not to be followed, and that the decision appealed from must be reversed, and the resolutions thereby declared to be ultra vires must be declared intra vires and valid. If, by declining to follow the second decision in Hutton v. Scarborough Cliff Hotel Co. (2), we were disturbing titles or embarrassing trade or commerce we should treat it as one of those decisions which, though wrong, it would be mischievous to overrule. But such is not the case; and it is desirable, from all points of view, to remove from

(8) [1894] A. C. 416, 417.

(1) 30 Ch. D. 376.

(2) 2 Dr. & Sm. 521.

(3) L. R. 19 Eq. 358.

companies a fetter which ought never to have been imposed upon them, and which in practice has been got rid of by skilled draftsmen by the insertion of power to issue preference shares in the original articles of association or the memorandum of association itself. These devices will no longer be necessary. We understand that there will be no dispute now as to the rights of the preference shareholders, and that the proper declaration will be as asked by the plaintiffs in the first paragraph of their claim. The costs will be provided for by the parties.^a

KENT v. QUICKSILVER MINING CO.

1879. 78 N. Y. 159.^a

THESE are appeals from judgments of the General Term of the Supreme Court, in the first judicial department, affirming judgments entered upon decisions of the court on trial at Special Term.

The action first entitled was brought to restrain, and the judgment therein did restrain defendant, The Quicksilver Mining Company, from converting or agreeing to convert the shares of its stock known as common stock into preferred stock, and from issuing any further preferred stock, and the individual defendants from converting any of the common stock into preferred stock. (Reported below, 12 Hun 53.)

The second action was brought for an accounting by said company, and for a distribution of the net earnings as follows: To pay first to the preferred stockholders seven per cent. per annum upon the amount of their stock, the residue to be divided pro rata among the holders of the common and preferred stock.

The third action was brought to restrain said company from paying, and the individual defendants, holders of preferred stock, from receiving, any sums as interest or as dividends in excess of dividends paid on the common stock; to restrain said company from issuing any further preferred stock; to have the preferred stock already issued declared illegal, and for an accounting and distribution of the net earnings equally among the stockholders. The judgment dismissed plaintiff's complaint, adjudged the preferred stock to be legal and valid, and its holders entitled to the preference it purported

^a See *Hazlehurst v. Savannah &c. R. Co.* (1871) 43 Ga. 13, 53; *West Chester &c. R. Co. v. Jackson* (1875) 77 Pa. St. 321, 327 (preferred stock "only a form of mortgage" where corporation has power to borrow on bond and mortgage); *Rutland &c. R. Co. v. Thrall* (1863) 35 Vt. 536, 546 (issue of preferred stock "a legitimate mode of borrowing money"); *Anthony v. Household Sewing Machine Co.* (1889) 16 R. I. 571, 18 Atl. 176, 5 L. R. A. 575 (money loaned to corporation to be repaid in preferred stock can be recovered, where corporation had no power to issue the stock).—Eds.

^b Portions of statement of facts and of opinion omitted.—Eds.

to give, and directed the said company to account and to distribute its net earnings accordingly. (The last two cases reported in 17 Hun 169.)

* * * * *

At the annual meeting of the stockholders of the company, held pursuant to notice as required by the by-laws, on the fourth Wednesday of February, 1870, the following amended by-laws and resolutions were adopted by a unanimous vote of 75,658 shares:

"By-law IV. Certificates of stock amounting to \$10,000,000 shall represent the value of the property of the corporation, and the capital stock shall be divided into 100,000 shares of \$100 each. Certificates of stock upon which five dollars (\$5) per share shall be paid, shall be distinguished as preferred stock.

"By-law No. XI. The preferred stock shall be entitled to interest at the rate of seven per cent. per annum, from the 1st of May, 1870, to be paid annually out of the net earnings of the company for each year. Should there remain a surplus of earnings after the payment of the said interest upon the preferred stock, then this surplus shall be divided pro rata among the holders of preferred and common stock, in proportion to their several interests.

"Resolved, That a preferred stock of the company be issued in shares of \$100 each, and that the treasurer be directed to open books at the office of the company in the city of New York, and to receive subscriptions to said preferred stock. Such subscriptions shall be received only from the holders of the common stock of the company on their surrendering to the company common stock, and paying to the treasurer five dollars on each share of stock surrendered.

"The common stock so surrendered shall be canceled before the issue of the preferred stock, share for share.

"Resolved, That the books for subscription to the preferred stock shall be closed by the board of directors whenever the interests of the company, in their opinion, will be promoted by so doing."

Books for subscription were accordingly opened, circulars containing the amended by-laws and resolutions were distributed to the stockholders, and notices were published in the New York daily papers. Owners of common stock to the amount of 42,913 shares subscribed for a corresponding number of shares of preferred stock, surrendered their said shares of common stock, and paid to the company the sum of five dollars on each share so surrendered; and the company thereupon issued and delivered to them certificates of shares of preferred stock, in which it was stated that such stock was entitled to the preference, specified in said amended by-laws. Since that time the two forms of certificates have been issued and continue to be issued by the company upon the surrender of like certificates for transfer; and the entire capital stock of the company, both common and preferred, has been transferred and the certificates thereupon surrendered and new certificates issued corresponding to those surrendered. Since May, 1870, the stock of the said company has been

regularly called at the Stock Exchange in the city of New York, and there openly bought and sold in the usual manner under two designations, viz.: "Quicksilver Common" and "Quicksilver Preferred," and upon such sales the price of "Quicksilver Preferred" has always been in advance of "Quicksilver Common," and reports of such calls, purchases and sales of said stocks have been regularly made by the Stock Exchange and published in the daily papers in the city of New York. The sum realized from subscriptions to the preferred stock was appropriated by the company to the payment of its current expenses, the interest on its mortgage debt and of judgments, for which the company was liable. At the annual meeting of the stockholders in February, 1871, the report of the president was submitted, stating that the by-laws authorizing the preferred stock were adopted at the last annual meeting by a unanimous vote of 75,658 shares, giving a complete copy of such by-laws, with a detailed statement of the amount received for subscriptions to the preferred stock and the disbursement of the same, and also showing the number of shares of common and of preferred stock. This report was by resolution approved, and the same with accompanying statement was directed to be published in pamphlet form for the information of the stockholders. Annual reports were presented and accepted at the annual meeting of the stockholders, held in the month of February in each of the years 1872, 1873, 1874, 1875, 1876 and 1877. Such reports were printed pursuant to resolutions adopted at the annual meetings, and were distributed to stockholders and other parties interested. At the annual meeting of the stockholders, held on the 24th of February, 1874, the following preamble and resolutions were adopted by a vote of 68,274 shares in the affirmative to 2,500 in the negative:

"Whereas, at a meeting of the stockholders, held February 24, 1870, a resolution was adopted giving the privilege of conversion into preferred stock to the holders of the common stock of the company upon the payment of five dollars per share for each share of common stock so converted, and that the option of such conversion was duly closed by the directors on the eighteenth of April following, at which time 42,913 shares of preferred stock had been issued as above provided.

"And, whereas, from the report of the president, submitted to this meeting, it seems desirable that previous to the payment of dividends the same privilege of conversion should be extended to the holders of the 57,087 shares of the common stock now outstanding, it is hereby

"Resolved, That the company will issue its preferred stock to the holders of the common stock of the company, share for share, upon the surrender of such common stock, and the payment, at the time of issue, of five dollars, and interest from February 24, 1870, upon each share of stock so surrendered.

"Resolved, That the common stock so exchanged shall be canceled previous to the issue of preferred stock, share for share.

"Resolved, That the directors be hereby authorized at their option, to close the books of the preferred stock for the purpose of this exchange whenever, in their judgment, the interest of the company will be promoted thereby, giving — days' notice previous thereto."

Previous to the sixteenth day of November, when the action of *Hoyt v. The Quicksilver Mining Company* was commenced, no suit or legal proceeding of any kind was brought by any common stockholder to restrain the issue of said preferred stock, or to have the same declared invalid, or to prevent the carrying out of the contract with the preferred stockholders; nor previous to the said meeting of stockholders in November, 1874, was any written protest or statement made in reference to the preferred stock, nor previous to that meeting was any serious or public objection to said preferred stock ever made, or any serious or public question as to its validity raised by any stockholder.

* * * * *

FOLGER, J.—These are suits in equity to perpetually restrain the Quicksilver Mining Company from taking certain action, on the one hand proposed by it with the expressed assent of some only of the stockholders in it; and on the other hand, demanded of it by certain other of the stockholders in it, which demand it and still other stockholders resist.

Whatever the frame of the pleadings in the several actions, and whatever the formal prayer for judgment, the purpose of the litigation in each is to reach a final and binding judgment, whether certain "preferred stock," heretofore created by that company, is so far valid as to be recognized in the future business of the company as giving to the holders thereof the peculiar right expressed in the certificate thereof.

What is meant by "preferred stock" is well enough known in law and business, without definition or circumlocution here.

All the powers which that company had were given to it by its charter (Laws of 1866, chap. 470, p. 1021); and by the Revised Statutes (vol. 1, pp. 599-600, §§ 1, 2, 3). Thereby it had the usual general powers of a corporation; (see Angell & Ames on Corporations, § 110.) It had also the peculiar power of holding, improving and working mining lands in California and elsewhere, and of disposing of the product thereof. It had also the power to issue certificates of stock, representing the value of its property, in such form and subject to such regulations as it might from time to time by its by-laws prescribe and to regulate and prescribe in what manner and form its contracts and obligations should be executed. It is claimed that it had also incidental and implied powers. So it had, so far as permitted by the Revised Statutes, which declare that in addition to the powers therein enumerated and to those expressly

given in its charter, it should not possess nor exercise any, except such as should be necessary to the exercise of the powers so enumerated and given. (1 R. S., 600, § 3.)

Plainly a mining corporation, for the exercise of its power of mining in its lands, must have money. Hence if it has it not, and cannot otherwise readily get it, it must, as necessary to the use of its corporate rights, have the power to borrow it; and in any way, and upon any obligation or security to be given by it, that is not unlawful. (Curtis v. Leavitt, 15 N. Y. 9.) It may borrow it from the stockholders in it, as well as from other parties; and it may determine and agree to borrow from them only. This corporation was in need of money to carry on its authorized business. It did get money, for that purpose and because of that need, from some of the stockholders in it; and in that instance from some of them alone. If the mode by which that money was got was a borrowing, within the sense which the law and common acceptance give to that term, then the transaction so far would have been lawful; and it would have remained to inquire whether the obligation given was a lawful instrument. But it was not a borrowing. The idea of a borrowing is not filled out unless there is in the agreement therefor a promise or understanding that what is borrowed will be repaid or returned; the thing itself or something like it of equal value, with or without compensation for the use of it in the meantime. To borrow is the reciprocal action with to lend; and to lend or to loan, say the dictionaries, is the parting with a thing of value to another for a time fixed, or indefinite yet to have sometime an ending, to be used or enjoyed by that other, the thing itself, or the equivalent of it, to be given back at the time fixed, or when lawfully asked for, with or without compensation for the use as may be agreed upon. In this transaction with some stockholders, that corporation had not the right, nor was it under the liability to ever pay back the five dollars per share furnished by them to it; that was not named in the terms of the obligation given, nor was it contemplated in the negotiation and bargain. The stockholder had not by the scope of his bargain, nor by the terms of the written evidence of it, any right ever to ask for repayment of the money furnished by him. In short, there was not formed thereby the relations of debtor and creditor. The stockholder parted forever with the money furnished, inasmuch as the charter of the company is perpetual, and the company made a perpetual charge upon its net earnings. Though there was compensation fixed for the use of the money, and though it was to take the form of a yearly payment, and at a rate the same as the then lawful rate of interest, yet we cannot conceive that the transaction was a loan and borrowing of money, with a compensation for the use of it. If it had been, though the compensation was great for the sum furnished, yet it was not a violation of the usury laws of which the corporation could avail itself (Laws of 1850, chap. 172); and the courts might not overhaul it; save, perhaps, as an unconscionable

and extortionate agreement (1 Story Eq. Juris., §§ 246-331); as to which we will speak again before the close. The transaction is not to be looked upon as other than a preference of one class of stockholders to another; as giving to the first class a perpetual inextinguishable prior right to a portion of the earnings of the company before the other class might have anything therefrom. It was none other than the creation of a "preferred stock".

Then there arises the query, whether there was at that time power in the corporation to distinguish between the stockholders in it, to form them into two classes, and to give to one class rights in the corporate property, business and earnings, from which the other was shut out.

We are not prepared to say that, at the first, the corporation might not have lawfully divided the interest in its capital stock into shares arranged in classes, preferring one class to another in the right it should have in the profits of the business. The charter gave power to make such by-laws as it might deem proper, consistent with constitution and law; and to issue certificates of stock representing the value of the property. We know nothing in the constitution or the law that inhibits a corporation from beginning its corporate action by classifying the shares in its capital stock, with peculiar privileges to one share over another, and thus offering its stock to the public for subscriptions thereto. No rights are got until a subscription is made. Each subscriber would know for what class of stock he put down his name, and what right he got when he thus became a stockholder. There need be no deception or mistake; there would be no trenching upon rights previously acquired; no contract, express or implied, would be broken or impaired.

This corporation did otherwise. A by-law was duly made, which declared the whole value of its property and the whole amount of its capital stock, and divided the whole of it into shares equal in amount, and directed the issuing of certificates of stock therefor. It is not to be said that this by-law authorized anything but shares equal in value and in right; or that the taker of one did not own as large an interest in the corporation, its capital, affairs, and profits to come, as any other holder of a share. Certificates of stock were issued under this by-law, that gave no expression of anything different from that. When that by-law was adopted, it was as much the law of the corporation as if its provisions had been a part of the charter. (*Presbyterian Church v. City of New York*, 5 Cow., 538.) So it is said in *Grant on Corporations*, page 80, in a qualified way. Thereby, and by the certificate, as between it and every stockholder, the capital stock of the company was fixed in amount, in the number of shares into which it was divisible, and in the peculiar and relative value of each share. The by-law entered into the compact between the corporation and every taker of a share; it was in the nature of a contract between them. The holding and owning of a share gave a right which could not be divested without the assent

was not
knowing
money
that
selling money
which it
never repaid
to give back
was act
n.v.

of the holder and owner; or unless the power so to do had been reserved in some way.] (Mech. Bank v. N. Y. and N. H. R. R. Co., 13 N. Y., 599-627.) Shares of stock are in the nature of *choses in action*, and give the holder a fixed right in the division of the profits or earnings of a company so long as it exists, and of its effects when it is dissolved. That right is as inviolable as is any right in property, and can no more be taken away or lessened, against the will of the owner than can any other right, unless power is reserved in the first instance, when it enters into the constitution of the right; or is properly derived afterwards from a superior law giver. The certificate of stock is the muniment of the shareholder's title, and evidence of his right. It expresses the contract between the corporation and his co-stockholders and himself; and that contract cannot, he being unwilling, be taken away from him or changed as to him without his prior dereliction, or under the conditions above stated. Now it is manifest that any action of a corporation which takes hold of the shares of its capital stock already sold and in the hands of lawful owners, and divides them into two classes—one of which is thereby given prior right to a receipt of a fixed sum from the earnings before the other may have any receipt therefrom, and is given an equal share afterwards with the other in what earnings may remain—destroys the equality of the shares, takes away a right which originally existed in it, and materially varies the effect of the certificate of stock.

It is said that when a corporation can lawfully buy property, or get money on loan, any known assurance may be exacted and given which does not fall within the prohibition, express or implied, of some statute (Curtis v. Leavitt, 15 N. Y. 66-67); and that is sought to be applied here. But the prohibition to such action as this is found, not indeed in a statute commonly so called, but in the constitutional provision which forbids the impairment of vested rights, save for public purposes and on due compensation. (The right which a stockholder gets on the purchase of his share and the issue to him of the certificate therefor is such a vested right.

It is contended that the power so to do is an incidental and implied power, necessary to the use of the other powers of the corporation, and is a legitimate means of raising money and securing the agreed consideration therefor. We have already conceded that it is legitimate to borrow money, and to secure the repayment of it, with a compensation for the use of it. But that is when it is done in such way as to put the burthen upon every share of stock alike, and to enable every share of stock to be relieved therefrom alike; in such way as to preserve the equality of right and privilege and value of the shares, and maintain intact the contract thereto with the stockholder.

Citations are made to us for the converse of this; but they do not come up—sometimes in their facts, sometimes in their declarations—to the necessity of the proposition. Either it is where the capital is

not limited and it is new shares that may be issued with a preference, and where there is express power to borrow on bond and mortgage (2 Redf. on R'ways, chap. 33, sec. 4, § 237; *Harrison v. Mex. R. W.*, 12 Eng. Rep. 793); or the amount of the capital stock has not been reached and such stock is issued therefrom (*Hazelhurst v. Savannah R. R.*, 43 Ga., 53; *Tottan v. Tison*, 54 id., 139); or there was legislative authority (*Davis v. Proprietors*, 8 Metcf., 321; *Rutland R. R. Co. v. Thrall*, 35 Vt. 545); or a restriction to authorized capital and there was unanimous consent of the stockholders (*Prouty v. M. S. and N. I. R. R.*, 1 Hun. 663; 43 Ga., 53, *supra*); or there was power to redeem, which was a transaction in the nature of a debt (*Westchester, etc., R. Co. v. Jackson*, 77 Penn. St., 321); or the opinion was *obiter* (*Bates v. Androscoggin R. R. Co.*, 49 Maine, 491); or it was the case of a subscription for stock with a condition for interest until the corporation was in operation (*Richardson v. Vt. and Mass. R. R. Co.*, 44 Vt. 613); or it was an action on a subscription more favorable to defendant than to other subscribers, and it was held that defendant could not set up the lack of equality (*Evansville R. R. Co. v. Evansville*, 15 Ind., 395); or a solemn determination of this question was not necessary for the disposal of the case (*Williston v. M. S. and N. I. R. R. Co.*, 13 Allen, 400); or the issue was authorized by the articles of association (*In re A'D. St. Nav. and Col. Co.*, 20 L. R. [Eq.], 339); or there was full knowledge on the part of all concerned (*Lockhart v. Van Alstyne*, 31 Mich., 81); or the power in the corporate body was conceded, and it was denied that it existed in the directors (*McLaughlin v. D. and M. R. R.*, 8 id., 100.)

We will not say, for we are not called upon here to say, that never can a corporation rightfully, against the dissent of a portion of its stockholders, make some of the stock preferred; what we assert is that this case does not present a state of facts in which a power so to do exists.

There is a power in this charter to alter, amend, add to or repeal, at pleasure by-laws before made. It is argued from this that it was in the power of the corporate body in due form and manner, to alter the by-law which had fixed the amount of the capital stock and the number and relative value of the shares thereof. The power to make by-laws is to make such as are not inconsistent with the constitution and the law; and the power to alter has the same limit, so that no alteration could be made which would infringe a right already given and secured by the contract of the corporation. Nor was the power to alter, to the extent of affecting the contracted relative value of a share, reserved when the share was sold to the stockholder, so as to enter into and form a part of the contract. An alteration is a *pro tanto* repeal; but no private corporation can repeal a by-law so as to impair rights which have been given and become vested by virtue of the by-law afterwards repealed. All by-laws must be reasonable and consistent with the general principles

of the laws of the land, which are to be determined by the courts, when a case is properly before them. (*The Master, etc., v. Green*, 1 Ld. Raym., 113). A by-law may regulate or modify the constitution of a corporation, but cannot alter it. (*Rex v. Cutbush*, 4 Burr., 2204; *R. W. Co. v. Allerton*, 18 Wall., 233.) The alteration of a by-law is but the making of another upon the same matter. If the first must be reasonable and in accord with principles of law, so must that which alters it. If then the power is reserved to alter, amend or repeal, and that reservation enters into a contract, the power reserved is to pass reasonable by-laws, agreeable to law. But a by-law that will disturb a vested right is not such; see *Gray v. Portland Bank* (3 Mass., 363; *Grant on Corps.*, 91). And it differs not when the power to make and alter by-laws is expressly given to a majority of the stockholders, and that the obnoxious ordinance is passed in due form.

It needs not that we consider the position that the issue of the preferred stock was an authorized increase of the capital and so legal. It did not profess to be; nor was it in fact. For each share of preferred stock given out, a share of common stock was taken in; so that the gross amount of the capital stock was still the same; and so were the number of shares and the nominal value of each share.

83c. We are therefore of the opinion that there was no power in the corporate body, nor in a majority of the stockholders, to provide by by-law for the creation of a preferred stock, so as to bind a minority of the stockholders not assenting thereto.

It is claimed that though there was not that power, as the facts now appear, yet that there was general authority conferred by charter to create such a stock; and that the regularity of the issue of it created a presumption of validity upon which subsequent purchasers had a right to rely, and which, in the present position of parties, can not be questioned.

It is a rule that the dealings of a corporation, which on their face or according to their apparent import are within its powers, are not to be regarded as illegal and unauthorized, without some evidence tending to show that they are of that character. (*Chautauqua Bank v. Risley*, 19 N. Y., 369.) It is another rule, that acts done by a corporation, which presuppose the existence of other acts to make them legally operative, are presumptive proofs of the latter. (*Nelson v. Eaton*, 26 N. Y., 410.) And it may be that where a corporate act is within the general power of the corporation, and its invalidity arises from something not apparent in the grant of power to the body, and which is extrinsic thereto, that one dealing with the corporation in ignorance of that which vitiates will not be affected thereby. We need not rest there, further than such principle is involved in the next topic which we consider. We have not definitely passed upon the question whether this corporation had power in the first instance to divide its stock into preferred and common; and that

would need to be settled before disposing of the proposition just noticed.

But there remains a serious question; whether, though there was at the outstart a minority of the stockholders who gave no assent to the corporate act, there has not been such tacit acquiescence and delay in action by that minority as to amount to indefensible *laches* and estoppel upon those who constituted it and their assigns. In our judgment there has; and we find here a safe place on which to rest our decisions of these cases.

* * * * *

In our view of the matter, a holder of common stock had an equitable right to restrain the privileged payment to a preferred stockholder from the profits of the company, and to have the contract therefor declared invalid. It was his duty to have been prompt in his application to the courts for that relief, before evil could fall upon innocent parties; and where application to the courts therefor has been delayed by his neglect, and advantages have been gained by the corporate body, assistance should be denied. (*Zabriskie v. Cleveland R. R. Co.*, 23 How. [U. S.] 395-398; *Evans v. Smallcombe*, 3 H. of L. Cas. [L. R.], 249.) It is said that the common stockholder should have some time in which to seek relief. It is enough to say in answer, that four years at least went by before a holder of common stock asked for the aid of the courts, and then not until a holder of preferred stock asked that aid to restrain proposed corporate action meant to put the common stock upon an equality with his own. * * *

*Judgments accordingly.*⁴

⁴ See also *Higgins v. Lansing* (1895) 154 Ill. 301, esp. 389-393, 40 N. E. 362; *Campbell v. American Zylonite Co.* (1890) 122 N. Y. 455, 25 N. E. 853, 11 L. R. A. 596 (unanimous consent of shareholders to preference necessary, in absence of express legislative authorization). Cf. *Banigan v. Bard* (1889) 134 U. S. 291, 10 Sup. Ct. 565, 33 L. ed. 932.

In *Hinckley v. Schwarzschild & Sulzberger Co.* (1905) 107 App. Div. (N. Y.) 470, 95 N. Y. Supp. 357, aff'g. (1904) 45 Misc. 176, 91 N. Y. Supp. 893, held that under the reserved power to alter and repeal, a legislative amendment providing for the issue of preferred stock on the consent of two-thirds of the capital stock is constitutional, though the law in existence at the time of corporate organization required unanimous consent. See also *Curry v. Scott* (1867) 54 Pa. 270, at p. 277.

In *People ex rel. Browne v. Koenig* (1909) 133 App. Div. (N. Y.) 756, 118 N. Y. S. 136, held, preferred stock may be deprived of voting power. Houghton, J., said: "Unless expressly forbidden by statute, the articles of incorporation may divide the stock into common and preferred, and may provide that the preferred stockholders shall be deprived of voting power in consideration of the preferences over the common stock which is given them. Such a provision is but an arrangement between two classes of stockholders, which does not concern the public, and does not violate any rule of the common law or any rule of public policy."—Eds.

SCOTT v. BALTIMORE & OHIO R. CO.

1901. 93 Md. 475, 49 Atl. 327.

Appeals from a *pro forma* decree of the Circuit Court for Baltimore City, dismissing the bills of complaint.

PAGE, J.—The main question presented in the two cases contained in these records involves the right of the preferred stockholders of the Baltimore & Ohio Railroad Company to share in the distribution of the net profits of the company that may be remaining after the appropriation of 4 per centum of the net earnings to the preferred stock. It is contended by the appellants that the preferred stockholder has not only the right to receive a dividend of 4 per centum out of the net earnings before any dividend shall be set apart for the common stockholders, but to share *pro rata* with the common stockholders in the distribution of the residue; or, as an alternative proposition, to share equally with the holders of the common stock in any part of the net earnings that may be distributable after the payment of a dividend of 4 per cent. each to the holders of both common and preferred stock. The legal title to both kinds of stock is now vested in trustees who hold it for five years, or for an earlier date in their discretion, with such powers and duties as are particularly described; and they have issued to the real owners of the shares "certificates of beneficial interest," which entitle the said owners to receive stock certificates for their shares, when the time the said trustees are to hold it shall expire, and in the meanwhile to receive payments equal to the dividends collected by the trustees.

The persons holding these "certificates of beneficial interest" are therefore the real owners of the stock and for the purposes of this opinion we may so regard them.

The question as to the relative rights of these two classes of stock cannot be answered by regarding only the characterization of one of them as "preferred;" because of the fact that this term, standing alone, means only a stock that differs from other stock in having a preference of some sort attached to it, without expressing the special nature of the preference.

Ordinarily the term "preferred stock" is understood to designate such stock as is entitled to dividends from the income or earnings of the corporation before any other dividend can be paid. 1 Cook on Stockholders, sec. 267; *Henry v. Great N. Railway Co.*, 1 De G. & J. 606. But, though this may be true, yet, to determine in each case the special properties and qualities it possesses, resort must be had to the statute or contract under which it was issued. "Preferred stock takes a multiplicity of forms according to the desire and ingenuity of the stockholders and necessities of the corporation itself." It is a matter of contract, Cook, section 269, or depends upon statute. *Heller v. Marine Bank*, 89 Md. 611.

It always, however, represents *pro tanto* the capital of the com-

pany, and has about it no elements or rights other than those that are conferred upon it by the statute or contract to the authority of which it owes its existence. In all other respects the preferred stockholder is upon the same footing as the common stockholder; he is not a creditor of the company; his stock represents the amount of his ownership in the capital; he may vote at the meetings of the company as the common stockholders may do, and in general terms do and perform such things and be subject to such obligations as the common stockholders are subjected to, except as the terms under which his preferred stock was issued, may preclude. *Mackintosh v. Flint, etc.*, R. R., 34 Fed. Rep. 582; *Re Barrow, etc.*, 59 L. T. R. 500.

The rights of the preferred stockholders are in the same manner limited or extended. The preferred dividends may be made cumulative or non-cumulative. The dividend may be a fixed amount for each year to be paid out of earnings, or it may be a percentage, not exceeding a certain amount to be determined by the directors at their discretion; and the preferred stockholder who has received his preferred dividend may still have a share of the net earnings that may remain. These are all matters for the determination of which the statute or contract must be looked to. The whole doctrine on this subject was summed up in a few words by the Lord Chancellor, when he said, in the case of *Henry v. The Great Northern Railway Co.*, 1 De Gex & Jones R. 636: "The expression 'preferred shareholder' is equivocal. It by no means clearly indicates what are the rights of those to whom it applies. I do not think it can fairly be said to be an accurate expression, whichever of the two constructions be put upon it. All which the language fairly imports is, that some preference is given to the persons to whom the language applies. How far the preference is to extend must be ascertained by other media than the mere expression itself." *Heller v. Marine Bank*, 89 Md. 610; *State, ex rel., Thompson v. C. & C. R. R. Co.*, 16 S. C. 530; *Warren v. King*, 108 U. S. 389; *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159; *Elkins v. Camden & A. R. R.*, 36 N. J. Eq. 236; *Gordon's Exr. v. R. F. & P. R. R.*, 78 Va. 501.

The solution of the question with which we are now dealing must depend therefore upon the construction to be placed upon the agreement of the parties expressed in the stock certificates. That must be taken as the embodiment of the contract, and the final expression of the entire measure of the dividend rights of the parties. *Greer v. Van Meter*, 54 N. J. Eq. 270. Evidence therefore of negotiations which preceded this final consummation of the agreement, or conversations as to the intentions of the parties, cannot be accepted, for the reason that all these are merged in the written instrument, which must be taken to express the final intention. *Bailey v. R. R. Co.*, 17 Wallace 96; *Cassard v. McGlannon*, 88 Md. 168; *Lazear v. Nat. Union Bank*, 52 Md. 78.

But evidence of the situation of the parties, the objects and

purposes for which the agreement was made, and, in a case like this, when it is important to decide whether the certificate contains the whole agreement, all the agreements and resolutions which preceded and authorized the issue of the stock, may be resorted to, for the purpose, not of altering the contract, but of arriving at the real intention of the parties as expressed in the written contract. 1 Cook on Stockholders, sec. 269, and authorities cited in note. In *Boardman v. Lake Shore & M. S. Railway Co.*, 84 N. Y. 173, the court said: "We think the whole proceeding relating to the issue of the stock may be taken into consideration as constituting one and an entire transaction. The resolutions were competent evidence to show authority to issue the stock; the proposal and other proceedings to carry out the purpose of the resolutions and the certificate as evidence of what stock was actually issued, and in part the terms upon which it was so issued. Altogether these papers evince what the intention was." *St. John v. Erie Ry. Co.*, 10 Blatch. 271; affirmed in 22 Wallace 136; *Rogers v. N. Y., etc., Land Co.*, 134 N. Y. 197; *B. & O. R. R. Co. v. Brydon*, 65 Md. 216; *Chicago, etc., R. R. Co. v. Denver & C. R. R. Co.*, 143 U. S. 596; *Mumford v. Memphis & C. Co.*, 2 Lea (Tenn.) 293; *First Nat. Bank v. Gerke*, 68 Md. 456.

But apart from this general principle which seems to be well established as we have stated, it is not important in this case, from the fact that all the instruments of writing relied on are connected together by reference one to the other. The certificate "of beneficial interest" and the certificate of stock refer to the resolutions of the company adopted on 14th April, 1899; these to the "proposition made by Mr. Vorhees," and this to the plan and agreement of reorganization, etc. So that a purchaser of a certificate of stock or of "beneficial interest" therein has had full notice of all these instruments of writing. They should therefore be regarded as instruments in *pari materia*, and may be resorted to to ascertain with precision whether the parties intended that the whole contract should be and was embodied in the certificate of stock. *Bailey v. Hannibal, etc., R. R. Co.*, 17 Wallace 96.

Having thus stated some of the general rules applicable to the matter before us, we will now proceed to examine the facts. The Baltimore & Ohio Railroad Company was incorporated by the act of 1826, ch. 123, of the General Assembly of Maryland. By the second section of the Act its capital stock was fixed at \$3,000,000, in shares of \$100 each; and by the thirteenth section, it was provided that if that proved insufficient for the purpose of the act, it was made lawful for the president and directors, etc., from time to time to increase the number of its shares, as they might deem necessary. This power was exercised from time to time, so that, when the company went into the hands of receivers in 1896, there were outstanding, of common capital stock to the amount of \$25,000,000, par value. The first issue of preferred stock, made under the act of 1835, ch. 395, was of \$3,000,000, par value, to the State of Maryland.

By the terms of the ninth section of that Act, the State as the holder thereof was entitled to receive "a perpetual dividend of six per centum per annum, out of the profits of the work as declared from time to time, and no more, etc." The second preferred stock amounting to \$2,000,000, was issued under the Act of 1868, ch. 471. This Act was amended by Act of 1880, ch. 471, and now remains in the Code as sec. 294 of article 23.

The holders of this stock are entitled to "a perpetual dividend of six per centum, and no more." So that in 1896 the capital stock of the company was:

Of common stock	\$25,000,000
Of preferred stock under the Act of 1835.....	3,000,000
Of preferred stock under the Act of 1868.....	2,000,000

Total.....	\$30,000,000
------------	--------------

In 1896 the company became insolvent, and in February of that year was placed in the hands of receivers appointed by a decree of the Circuit Court of the United States for the District of Maryland.

The aggregate amount of the company's obligations, secured by mortgages and otherwise, or non-secured, were very large, and amounting to many millions and during the three years of the receivership the amount of the obligations was increased by the issuance of receivers' certificates which became liens on the road and its earnings to the extent of over five and a half millions of dollars. In June, 1898, a plan for the reorganization of the system was devised by a committee created for that purpose.

It is impossible to examine this plan (a copy of which is to be found in the record) without being impressed with the business skill of its framers. It was manifestly intended and seems to be a comprehensive document, which should cover every possible contingency that a careful examination and much intelligent thought could suggest. There is apparent a most thorough and exact knowledge of the affairs of the company, and a full appreciation of the magnitude of the interests with which they proposed to deal. It is most carefully and skilfully devised and was formulated into words and phrases evidently by some one who was expert and intelligent in the performance of such work. Its aim, as is set forth in its provisions, was to prepare a plan for reorganization which should not only bring the fixed charges within the earning capacity of the road, and secure the payment of the floating debts and existing obligations, but also to provide "adequate capital" for the "present and future requirements of the road." When it is borne in mind that the problem before them involved the adjustment upon just and equitable principles of the various and doubtless conflicting interests of many persons, the complicated and multifarious relations of the properties of other companies and the combination of all these varied interests in one harmonious plan, it is difficult to conceive how in one of its most important features there should have been left anything to con-

struction. The plan provided for contemplates the issue of three kinds of securities with which the old indebtedness was to be settled for; viz:

- 1st. \$70,000,000, prior lien, $3\frac{1}{2}$ per cent. gold bonds, due 1925.
- 2nd. \$63,000,000, fifty year 4 per cent. gold bonds.
- 3rd. \$40,000,000, 4 per cent. non-cumulative preferred stock.
- 4th. \$35,000,000, common stock.

Each of these several securities and the purposes of their creation, and how they are to be applied, etc., are carefully described in the plan. It is also provided that no additional mortgage shall be put upon the property and no increase in the amount of the preferred stock, except with the consent of both classes of stock, voting separately. Is it within the bounds of reason to suppose that if it was intended that this large amount of preferred stock was to have the right, to the great injury of the common stock, to share in the surplus of net profits remaining after it has received its 4 per cent. dividend, that these careful business men would not have had it definitely so expressed in the plan? There is nothing in the condition of the law that could have warranted the omission. Whatever courts may hold eventually as to the right of ordinary preferred stock to share in the residue of net earnings after its preferred dividend has been received, the maintenance of that right in the absence of anything in the contract creating such preferred stock, so far as we are informed, has not yet been taken by any court. No decision holding this has been furnished us by the very able and industrious counsel who argued this case for the appellant, and we have found none ourselves. It is true that some of the text writers do intimate that such may be the law, but the cases cited are those where there is express provision for the participation in the surplus, and fall far short of sustaining the proposition by which the appellants here seek to impose the additional quality upon the preferred stock. One of these cases is *Bailey v. Hannibal, etc., Railway Co.*, 17 Wallace 96. There it was expressly provided that after the preferred dividend the stock should be entitled to "an equal dividend with said other shares," etc. A like provision is to be found in the other case cited. *Allen v. Londonderry, etc., R. R. Co.*, 25 W. R. 524.

So that there is no room here for the argument that in declaring the rights of the preferred stock it was not necessary to state particularly that it should have such attributes, because of the reason that under well-settled principles of the law it is entitled *proprio vigore* to such participation. And although it were conceded that the right of the preferred stockholder, after he has received his preferred dividend, to participate in the surplus net earnings can be supported by cogent reasoning, yet in a case like this where so much exactness of detail is observable in the plan, where the interests involved are so great, and where the proposition of law has not been definitely settled but lies in the mind of each person as he may reason out the matter for himself, it would be most unreasonable to assume that

when the schedule for the issue of \$40,000,000 of preferred stock was included in the plan, everything was not then put there that the parties intended should be there. It was necessary, in the highest degree, that each class of new issues should be properly described. The description of the new mortgages and the total amounts they were to cover was carefully complete. As to the common stock, it was not necessary that its characteristics should be stated for they were definitely fixed by law. But it was supremely necessary in reference to the preferred stock, to make such description of it as would clearly inform its holders of just what rights would attach to its ownership. It was necessary to state that it was to be non-cumulative and entitled to a preference dividend not exceeding 4 per cent.; otherwise it would have stood on the same footing as the common stock. The holders of practically all the shares of capital stock deposited their securities and accepted the new stock, whereby they "assented to" the issue of the preferred stock and are not now in a position to object to the validity thereof. It is clear that the new stock was issued, not under any statute specially authorizing such issue, but solely under the general power of the corporation to issue such stock as all of its stockholders shall direct to be issued, that is by the express agreement of all of its stockholders. To construe this express contract, as set out in the certificate, when read in connection with the resolutions of the directors of April 11th, 1899, and the other papers referred to directly and indirectly in the resolutions, as being incomplete and fragmentary, so that its true meaning cannot be ascertained without reading into its provisions that are, at least, doubtful in law and certainly not sustained by any proof in the case, would do violence to the principles applicable to the construction of written instruments, as have already been herein set forth.

Is there anything in the language employed in the certificate which would require a different construction than that we have given to it? The contract as set forth in the certificate of the preferred stockholder, is: "The holders of preferred stock to the amount now issued and such additional amounts as may be lawfully issued from time to time by the President and Directors of the Company, pursuant to the resolutions of the stockholders duly adopted April 11th, 1899, are entitled to receive in each year, out of the surplus net profits of the company for the current year such yearly dividend (non-cumulative), as the Board of Directors of said Railroad Company may declare, up to, but not exceeding, four per centum, before any dividends shall be set apart or paid upon the common stock." The certificate of the original preferred stock, issued under the acts of 1835 and 1868, provided that the preferred stockholder should have a "perpetual dividend of six per centum per annum and no more," and it is insisted that the omission of the words "no more" is significant, as indicating the intention of the parties. But the case of the original preferred stock is different from the one with

which we are now dealing. The pre-existing preferred stock was issued to conform to the requirements of the statutes of 1868 and 1835. Both of the statutes contained the words "no more," and it was perhaps proper that they should be there, so that the intention of the legislature should be clearly expressed. Here the preferred stock was issued with the assent of all the stockholders and to carry out a plan of reorganization. It was the intention of all the parties that the new preferred stock should be issued to carry out the plan of reorganization and that it should have such preferences, rights and attributes as were contemplated by the plan. There was no necessity, therefore, for the use of the words "no more," because by the plan and the resolutions of the company, passed April 10th, 1899, the preferred stock was to be "entitled to receive non-cumulative dividends at the rate of four per centum per annum before the payment of any dividend on the common stock, but shall have no lien upon the property of the company." The omission of the words "no more," therefore, we do not think is a matter of any significance whatever. The words of the plan, referring to the preferred stock, are as follows:

"\$40,000,000 4 per cent. non-cumulative preferred stock per annum before the payment of any dividend on the common stock." If these be compared with the words contained in the certificate of the stock there will be found a slight difference. In the latter certificate it is provided that the preferred stock is entitled to receive out of the surplus such yearly dividend (non-cumulative) as the board may declare "up to, but not exceeding four per centum before any dividends shall be set apart or paid upon the common stock." Why were the words "not exceeding" thus inserted? What is their significance? If it was only to indicate that the 4 per cent. was the largest amount that could be received before the common stock was entitled to a share of the earnings, the words "up to" would have been quite sufficient and the other words would have been surplusage. But we cannot neglect these words, for in construing a contract it is not to be presumed that words are lightly used, but each word should be given due weight. "A word not plainly inserted by accident or mistake is never to be thrown out entirely while there is a plain and natural construction which can be given to it not manifestly destructive of the general intent of the sentence." *Philadelphia v. River Front R. Co.*, 133 Pa. St. 134.

If it be conceded that the purpose of the certificate was to express what share of the net earnings the preferred stock was to be entitled to, it is possible to give the words "not exceeding" some force; but not otherwise. The certificate would then mean, that it was to receive 4 per cent. and nothing exceeding that proportion: the said amount to be received before any dividends be allowed to the common stock. Upon the hypothesis of the appellant that the whole purpose of the certificate was to declare what the preferred stock was entitled to, before the common stock would be entitled to receive anything, the words "not exceeding" perform no function

whatever. The certificate states what the preferred stock "will be entitled to receive;" and that is, "not exceeding four per cent." That is the measure of its rights, and if so, how is it possible to hold that having received that amount before the common stock received anything, it shall yet receive afterward, an additional sum? According to the fair meaning of these words, it seems to be clear that a proper construction of them and the only one that will harmonize them all is that the preferred stock should be non-cumulative and should receive 4 per cent. and no more, out of the net earnings; but should be entitled to receive that before any dividends are set apart for the common stockholders.)

It follows that the decrees must be *affirmed* in both cases.*

Section 7.—Overissue of Stock. Watered Stock.

CLARK v. TURNER.

1884. 73 Ga. 1.

The Grangers' Life and Health Insurance Company brought suit against J. W. Turner and Abner Echols for \$250.00, as an assessment of ten per cent. on a stock subscription of \$2,500.00, on which \$250.00 was paid and a note given for the balance of \$2,250.00, dated August 10, 1875, payable on demand without interest, "in part consideration for twenty-five shares of the capital stock of said company, subscribed for by John W. Turner, subject to the conditions and regulations in the constitution of said company in regard to stock notes."

Defendant, Turner, pleaded the general issue and a special plea, to the effect that the plaintiff was incorporated under a declaration

* See *People ex rel. Cantrell v. St. Louis & C. R. Co.* (1898) 176 Ill. 512, 45 N. E. 824, 52 N. E. 292; *Field v. Lamson & C. Mfg. Co.* (1894) 162 Mass. 388, 38 N. E. 1126, (see note 27 L. R. A. 136); *Warren v. King* (1882) 108 U. S. 389, 2 Sup. Ct. 789, 27 L. ed. 769; *Hamlin v. Toledo & C. R. Co.* (1897) 78 Fed. 664, 24 C. C. A. 271, 36 L. R. A. 826 (valuable opinion *per* Lurton, J.).

In the case first cited, Magruder, J. said: "In estimating the liabilities of the Belleville and Eldorado Railroad Company, certain indebtedness, which is in the nature of preferred stock, is charged up as a liability, in the accounts produced, to show that the obligations of appellee are such as to relieve it from the duty of operating the passenger train asked for. This is manifestly improper, because guaranteed or preferred stock is but a dividend and not a debt, and the holder of a certificate for such stock can have no action against the company as for a debt, but his right is to a dividend."

Where there is provision for preferential dividend, but no provision for division of capital, on winding up, preferred and ordinary shareholders share equally and assets must be distributed without regard to their rights in respect of dividend. In *re* London India Rubber Co. (1868) L. R. 5 Eq. Cas. 519, *per* Malins, V. C. Cf. In *re* Bangor & C. Slab Co. (1875) L. R. 20 Eq. Cas. 59, *per* Malins, V. C.—Eds.

of incorporation filed in the office of the probate court of the county of Mobile, Ala.; that under this declaration, the capital stock of the company was limited to \$100,000.00; that a general statement that it desired to have the privilege of increasing the capital had been decided by the courts of Alabama not to be sufficient to give any right of increase under the laws of that state; that the entire amount of capital was subscribed for, but afterward, nevertheless, the plaintiff represented to this defendant and others that it had the right to increase its capital to \$200,000.00, and obtained from him a subscription to \$2,500.00 of the stock of the company; that he paid the ten per cent. required, and gave the note in suit for the balance, with Echols as security; that this subscription was ultra vires and void, and the note given therefor was not collectable.

Plaintiff having assigned its property to Clark, he was made the party plaintiff in its stead. The case was submitted to the presiding judge without a jury. The plaintiff introduced the note sued on, having on it a credit of \$25.00 for a dividend, January, 1877, and showed the assessment of ten per cent. on subscribers; also that there was an outstanding judgment against the company for \$2,000.00 principal, recovered by one Mrs. Deppish on a policy issued on her husband's life after the date of Turner's subscription, and that a return of nulla bona had been made on the fi. fa.; also that the company had assigned to Clark. A witness testified that Turner had been appointed a trustee of the company, and he thought had acted as such. Under the constitution of the company, the president and secretary of the company, with the approval of the board of directors, could establish branch departments in different states and appoint a board of trustees for such branch departments, and they, in turn, should annually elect a board of directors of the branch; each trustee was also empowered to receive applications for insurance.

The charter and constitution of the company were before the court. He found for the defendants on the pleas of the general issue and the invalidity of the subscription. Plaintiff moved for a new trial, on the ground that the finding was contrary to law and evidence. The motion was overruled, and plaintiff excepted.

JACKSON, CHIEF JUSTICE.

This suit was brought by the Grangers' Life and Health Insurance Company of the United States of America, a corporation created by virtue of the laws of the state of Alabama, against John W. Turner, for the recovery of a ten per cent. instalment called for on a promissory note for stock therein. The defendant set up by plea that the corporation was permitted by the laws of Alabama to issue stock only to the amount of one hundred thousand dollars, which had been exhausted by the issue of stock to that amount prior to his subscription, and therefore the issue of more stock was ultra vires and void, and if he paid his subscription, he would get nothing therefor. The entire case, on law and facts, was submitted to the

presiding judge without a jury; the judge rendered a decision for the defendant, and the assignee of the corporation having been made a party, excepted, and assigns that judgment for error here.

It seems clear from the evidence that the stock was limited to one hundred thousand dollars in the application for and grant of the charter, under the general laws of Alabama, by the proper court of that state. There was some sort of reservation of the right to issue more in this application, but nothing was done by the court in respect thereto, nor was any authority granted to the corporation to issue more, under the laws of Alabama.

Indeed, in the case of this same company against Kampes et al., decided by the Supreme Court of Alabama at the December term, 1882, it was held that, under the general law of Alabama and the amendments thereto and the charter of this company by the Mobile court, there was given it no power to go beyond the sum of one hundred thousand dollars; that the issue of stock beyond that amount was ultra vires and void, and consequently that the subscription beyond that sum could not be collected. A certified copy of the opinion in that case is before us, the case not having been yet reported and published, and that judgment must control and conclude this case.¹ The Alabama decision upon its own statute law is respected in the sister states of the Union, and would be recognized as giving the true intent and scope of her statute law by the Supreme Court of the United States. The latter court, in the case of *Scovill v. Thayer*, 105 U. S. 143, announces the same principle as is decided in the case of this corporation by the Alabama decision, in a similar Louisiana case, and holds stock beyond an amount authorized by the laws of Louisiana utterly void and uncollectible by judicial process, ruling that subscription to such stock created no privilege or right in the subscriber and no liability on his part. If this subscriber had induced insurance on the part of any person in the Grangers' Life and Health Insurance Company by his acts as trustee or agent, or on the faith of his subscription, then an action on his individual right for the tort against Turner would lie; but this assignee stands in the shoes of the corporation and sues for the benefit of all creditors, and there is no pretense in this record that any particular creditor was induced or influenced by his action to insure in the company. *Scovill v. Thayer*, supra. So that neither the corporation nor its general assignee can recover in this suit, on the facts which this record discloses. In the cases of *Turner v. The Grangers' Life and Health Insurance Co.*, 65 Ga. 649, and *Hamilton v. the same*, 65 Ga. 750, and 67 Ib. 145, this plea of ultra vires was not in issue, but the parties against this corporation in those cases relied upon false and fraudulent representations on the part of the company as inducing their subscriptions as the ground of their defense, and their action in reference to this company

¹ See *Granger's Life & Health Ins. Co. v. Kamper* (1882) 73 Ala. 325, per Bricknell, C. J.—Eds.

and their subscriptions therein. So that neither of those cases touch the decision now made. For the first time, this point is now made in this court, and, as seen above, the judgment by the Supreme Court of Alabama, in the case of this company v. Kampes et al., supra, absolutely controls and concludes this case, that judgment being a construction of the power of an Alabama corporation under its statutes.

*Judgment affirmed.*²

IN RE ALMADA AND TIRITO CO.

1888. L. R. 38 Ch. Div. 415.³

THIS was a motion by T. C. Allen, a shareholder in the Almada and Tirito Company, Limited, to rectify the register of the company by striking his name off in respect of certain shares which had been issued to him under the following circumstances:

The company was incorporated on the 1st of April, 1885, as a limited company under the Companies Act, 1862, with a capital of

² That over-issued stock is a nullity and the shares are void, see N. Y. &c. R. Co. v. Schuyler (1865) 34 N. Y. 30. Davis, J. at page 49 said: "One of these is the question whether the stock purporting to be created by the false certificates and fraudulent transfers of Schuyler can be valid stock of the corporation and become part of its capital. In the nature of things this is impossible. A corporation with a fixed capital divided into a fixed number of shares can have no power of its own volition, or by any act of its officers and agents, to enlarge its capital or increase the number of shares into which it is divided. The supreme legislative power of the State can alone confer that authority and remove or consent to the removal of restrictions which are part of the fundamental law of the corporate being; and hence every attempt of the corporation to exert such a power before it is conferred, by any direct and express action of its officers is void; and hence every indirect and fraudulent attempt to do so is void; for if such a result cannot be accomplished directly by the whole machinery of the corporate powers, it is absurd to suppose that it can be produced by the covert or fraudulent efforts of one or more of the agents of the corporation. The Special Term was, therefore, right in holding that the spurious stock, attempted to be created by Schuyler in excess of the capital, formed no part of the capital stock of the company, but was utterly invalid; and it necessarily followed from the decision of this court when the case was before it on demurrer, that the plaintiffs were entitled to have all certificates and transfers which represented such spurious stock declared void and ordered to be canceled." Cf. Knowlton v. Congress &c. Spring Co. (1874) 57 N. Y. 518.

In Spring Co. v. Knowlton (1880) 103 U. S. 49, 26 L. ed. 347, held that one who had paid part of his subscription to a new issue of stock increased in violation of law could recover back the amount paid, on the theory that he was suing to recover in disaffirmance of an illegal contract.

In American Tube-Works v. Boston Machine Co. (1885) 139 Mass. 5, 29 N. E. 63, followed in Reed v. Boston Machine Co. (1886) 141 Mass. 454, 5 N. E. 852, held that the holder of stock illegally issued does not become a member in respect to such shares and can recover back money paid for them. In Scovill v. Thayer (1881) 105 U. S. 143, 26 L. ed. 968, held that the holder of over-issued stock was not liable to creditors. Cf. Palmer v. Bank of Zumbrota (1898) 72 Minn. 266, 75 N. W. 380.—Eds.

³ Opinion of Cotton, L. J., omitted.—Eds.

£210,000 in 210,000 shares of £1 each. The object of the company, as stated in the memorandum of association, was to acquire and work the property and undertaking of a previously existing company called the Almada and Tiritó Consolidated Silver Mining Company.

The articles of association adopted the regulations of Table A in the Schedule to the Companies Act, 1862, and provided, that the company might reduce its capital in the manner and with any of the incidents prescribed or allowed by the Companies Acts, 1867 and 1877; and that the company might accept surrenders of shares, but might not expend any part of its assets in purchasing the company's own shares.

A resolution was passed at a special general meeting of the company on the 6th of June, 1887, and confirmed at a subsequent meeting of the 22nd of June, "That the capital of the company be increased from 210,000 shares of £1 each to 420,000 shares of £1 each, by the issue of 210,000 shares of £1 each credited with 18s. per share paid, with a deposit of 6d. per share."

Shares to the amount of 74,327 were applied for under this resolution, of which Allen applied for 200, and the applicants paid a deposit of 1s. on each share.

On the fourth of January, 1888, an agreement was executed between the company on the one part and J. A. Morgan on behalf of the subscribers for the new shares on the other part, witnessing that the company should forthwith have the agreement filed with the Registrar of Joint Stock Companies, and that the company should forthwith, after the filing of the agreement, allot and issue to the subscribers whose names were inserted in the schedule, in pursuance of their applications, the number of the shares set opposite their names in the schedule; and that the shares should be issued and held as shares of £1 each, with 18s. per share credited as paid up thereon, making, with the deposit of 1s. per share, the sum of 19s. paid up on each share.

This agreement was registered with the Registrar of Joint Stock Companies on the same day. No certificates of the new shares had been issued.

On the 24th of January, 1888, Allen having become acquainted with the decision of the Court in *In re Addlestone Linoleum Company* (1) moved before Mr. Justice Chitty, under the 35th section of the Companies Act, that the register of members of the company might be rectified by striking out his name, and that the money paid on his shares might be returned to him; the ground of his application being that the issue of shares at a discount was *ultra vires* and void.

Mr. Justice Chitty, following his own decision in *In re Ince Hall Rolling Mills Company* (2) held that the issue of the shares was

(1) 37 Ch. D. 191.

(2) 23 Ch. D. 545, n.

valid, and dismissed the application with costs. Allen appealed from his decision.

It was agreed between the parties that the result of the application should depend upon the validity of the contract between the company and the shareholders, and that no question should be raised as to the form of the application.

Fry, L. J. :—The question which we have to solve is, I think, simply and shortly answered by a reference to this inquiry—What is the nature of an agreement to take a share in a limited company? In my opinion it is an agreement to become liable to pay to the company the amount for which that share has been created. Further, it appears to me to be clear that the liability of the shareholders is limited only by the amount unpaid on the shares. Now, observe, it is the amount unpaid; it is not the amount remaining due. The result is that a release by the company will not diminish the liability—accord and satisfaction between the company and the shareholder will not diminish the liability; nothing will diminish or extinguish that liability but payment. The consequence is that we are driven to this second short inquiry, Is an agreement to take 2s. for 20s. a payment of 18s.? I say it is not. That appears to me to be the whole matter.

Then a supplemental question is raised in this way: it is said that however it stood under the Act of 1862, the result is altered by the 25th section of the Act of 1867. That section is in these words:—[His Lordship read the section.]* What the exact words to which “the same” refer may be, it is a little difficult to ascertain; but I think the view suggested by Mr. Phipson Beale is the true one—that it means unless terms of payment otherwise have been determined.

Then we come to the inquiry: Is an agreement to take 2s. for 20s. a term or mode of paying 18s.? I have already said that in my judgment it is not a payment of 18s. It, therefore, cannot be a term or mode of payment. Consequently the registration of this agreement, which is an agreement in effect to release the 18s., is entirely inoperative under the 25th section of the Act of 1867. When we have determined this question the rest of the matter is arranged between the parties. Mr. Beale has, I think very properly, not thought fit to argue whether such a contract as this, entered into under a common mistake of law, is or is not capable of being rescinded, or whether the 1s. can be claimed as damages. It has been agreed between the parties that the result of this application is to depend upon our decision as to the real nature of the contract.

LOPES, L. J. :—I entirely agree with the judgments which have been delivered, and I will in a very few words express my views.

*“Every share in any company shall be deemed and taken to have been issued and to be held subject to the payment of the whole amount thereof in cash, unless the same shall have been otherwise determined by a contract duly made in writing, and filed.”—Eds.

Every limited company is required to state in its memorandum the amount of capital with which it proposes to be registered divided into shares of a certain fixed amount. Now, to my mind, this cannot be intended to be an idle or objectless requirement; but the amount of the share is to be the real sum to be paid, either in cash or, subject to the restrictions of sec. 25, in kind, which the company contracts to accept as of that cash value. In sec. 25 there can be found no provision of any sort or kind except the shares being paid up in full. I can see no practical distinction between issuing shares at a discount and returning to the member a portion of the capital to which the creditors have a right to look as that out of which they are to be paid. Issuing the shares at a discount, to my mind, would be rendering one of the statutory requirements of the Act an empty form. The case of *Trevor v. Whitworth* (3) has been referred to, and it appears to me that the reasoning and the decision in that case is applicable here. Another case referred to was the case of *In re Addlestone Linoleum Company* (4), where no doubt the question of whether the shares might be issued at a discount was not directly raised, but there are expressions of opinion by Lord Justice Cotton and Lord Justice Lindley, with which I concur, entirely in harmony with the decision at which the Court has now arrived. I am of opinion, therefore, that there is no power to issue these shares at a discount, and that the names of the shareholders in question must be removed from the register.⁵

STEIN v. HOWARD.

1884. 65 Cal. 616, 4 Pac. 662.

APPEAL from an order of the Superior Court of the city and county of San Francisco, refusing an injunction.

The Spring Valley Water Works, a corporation, was organized in 1858, and the proceedings for the increase of stock, mentioned in

(3) 12 App. Cas. 409.

(4) 37 Ch. D. 191.

⁵*In re Plaskynaston Tube Co.* (1883) L. R. 23 Ch. Div. 542 and *In re Ince Hall Rolling Mills Co.* (1882) L. R. 23 Ch. Div. 545, n., *per Chitty, J., contra*, overruled by the principal case.

Oregum &c. Min. Co. v. Roper, A. C. (1892) 125: *Held*, in a suit by stockholders of a solvent company that the allottees of stock issued at a discount held it subject to the liability to pay the company the full amount of the par value of the stock in cash.

Welton v. Saffery, A. C. (1897) 299: *Held*, it being *ultra vires* for a limited company to issue shares at a discount or by way of bonus, the holders of shares so issued are liable for the amounts unpaid on their shares not only to the creditors, but also for the adjustment of the rights of the stockholders among themselves. *Cf. Winston v. Dorsett Pipe & Paving Co.*, 129 Ill. 64, and cases *infra*, note 9.—Eds.

the opinion of the court, were taken in accordance with the Statute of 1853, which was in force at the date of the incorporation. The other facts are stated in the opinion of the court.

MYRICK, J.—The complaint in this case was filed by a stockholder for the purpose of enjoining the trustees of the Spring Valley Water Works, a corporation, from issuing and selling twenty thousand shares of stock. The capital stock of the corporation was eight million dollars, divided into eighty thousand shares, of the nominal value of one hundred dollars each. At a meeting of the stockholders, duly called, held on the 6th day of July, 1876, it was resolved (more than two-thirds of the capital stock being represented, and the vote being unanimous as to all present) that the capital stock be increased to sixteen million dollars, to be divided into one hundred and sixty thousand shares of one hundred dollars each. At a regular meeting of the board of trustees held April 1, 1884, it was resolved by the board that the president and secretary be authorized to issue and sell twenty thousand shares of the increased stock of the corporation at eighty-seven and one-half dollars per share, the stockholders to be entitled to purchase one share of stock for every four shares which they then owned. The answer of the defendants averred that the corporation had already expended and paid out, in the construction of its works, and in the purchase of property necessary therefor, a sum of money in excess of the eight million dollars, for which certificates of stock had been issued, and of two million dollars, for which the proposed certificates were to be issued, and that the increase of the stock was bona fide, and for the purpose of selling the increased stock from time to time to raise funds for the purpose of extending and increasing the capacity of the works of the corporation; that for the protection of the property of the inhabitants of the city and county of San Francisco, and for supplying said inhabitants with an abundance of water, it had become, and was necessary, that the property and capacity of the works of the corporation should be at once increased; and that the corporation had already entered into contracts involving the expenditure of more than half a million dollars for the purchase of property necessary to the extension and increase, and that it was necessary to construct a new aqueduct and line of pipe for more than twenty-five miles; that the contemplated expenditure would amount to two millions of dollars; that for a long time past the stock of the corporation had fluctuated in the market, some days being as low as eighty-three dollars, and other days as high as ninety dollars per share, and that on the said 1st day of April, 1884, the market value was eighty-seven and a half dollars per share, and no more; that the proposed sale of the increased stock was for the purpose of raising funds for the purposes aforesaid, and that the price named is the highest price which can be obtained.

The Civil Code of this State, section 359, makes provision for an

increase of the capital stock of an incorporation. The Constitution of this State contains the following prohibition in article xii., section 11: "No corporation shall issue stocks or bonds except for money paid, labor done, or property actually received, and all fictitious increase of stock or indebtedness shall be void." The question for decision on this appeal is, whether the stock proposed to be issued and sold will create a fictitious increase of stock. Webster's Dictionary defines the word "fictitious" to mean feigned, imaginary, not real, counterfeit, false, not genuine. The circumstances under which the stock is proposed to be issued and sold, as above stated, are, that the corporation has actual need of money for the purposes of its business, that the stock is proposed to be sold at the actual market-value of the stock of the corporation, and to be sold only in such quantities as may produce the requisite funds. (Under such circumstances, we think, it cannot be held that the issue is fictitious.) Perhaps it might be asked at what price should stock be offered for sale in order to make the issue fictitious. We apprehend that no direct and positive answer can be given. The Constitution has given no definition of the word "fictitious;" it has not declared what was meant by the use of that word, further than what the word itself implies, taken in connection with the context. We apprehend that in ascertaining the purport of the word, or rather its application, we must take into consideration the surrounding circumstances. Of the stock proposed to be issued there is no one share upon which a person can place his finger and say that share is or will be feigned, imaginary, not real, counterfeit, false, not genuine. Each share is offered at a price equal to the price of any one of the old shares. So far from the new shares being fictitious as to the old shares, it may be that burdens which would otherwise rest on the old shares, to wit, the payment of the corporation debts, will be entirely removed by the application of the funds realized, or shared in pro rata by the new shares. We cannot say but that this removal of such burdens, or the sharing therein, will be of the value of the discount in the price at which the new shares are proposed to be sold, or increase the actual value of the old shares to their par value. It may very properly be said that the use of the word "fictitious" in the Constitution, as above quoted, was as in contrast with the preceding sentence—as if to say, that stock issued for money paid, labor done, or property actually received (price not named) is not fictitious.

We do not think the issue or sale of the stock in question is within the prohibition of the Constitution. *Order affirmed.*

MORRISON, C. J., ROSS, J., SHARPSTEIN, J., and MCKINSTRY, J., concurred.*

* Cf. *Kraft v. Griffon Co.* (1903) 82 App. Div. (N. Y.) 29, 81 N. Y. S. 438. *GARRETT v. KANSAS CITY COAL MIN. CO.* (1892) 113 Mo. 330, 20 S. W. 965, 35 Am. St. 713. Suit to compel defendant corporation, its shareholders and directors, to issue to plaintiff certain shares of stock, which according to the

MORROW v. IRON & STEEL CO.

1889. 87 Tenn. 262, 10 S. W. 495.¹

LURTON, J.: The Nashville Iron, Steel & Charcoal Company is a manufacturing corporation, organized in 1887, under the general incorporation law of this State. Complainant's bill charges that it was organized upon the following scheme or basis, namely:

"The capital stock was fixed at \$350,000, in shares of \$100 each; the company was also to issue \$350,000 of \$1,000 negotiable, interest-bearing coupon bonds, to run twenty years, secured, principal and interest, by first mortgage, in the usual form, upon the company's plant. Every subscriber was to have bonds and also stock of the company, each to the amount of the subscription—that is to say, a subscriber to the amount, say of \$1,000, was to pay \$1,000, and therefor was entitled to and was to receive \$1,000 of said bonds and \$1,000 of said stock of the company."

Complainant alleges that "upon this basis and plan of operations, as the defendant company well knew, your orator subscribed for \$10,000 of said stock and bonds each—that is, he took an interest to the extent of and subscribed \$10,000, and he was to pay the said \$10,000 upon calls to be made."

Upon this subscription he afterward paid \$1,000, and executed his three negotiable notes each for \$3,000, and payable in March, April, and May, 1888. Subsequently the corporation refused to carry out the scheme by which subscribers were to receive bonds to an amount equal to their stock, and instead resolved to mortgage their property only to the extent of \$100,000, and these bonds they resolved to sell upon the market, applying the proceeds to corporate purposes strictly. This change in the plan of operations seems to have been assented to by all the subscribers save complainant, who caused his protest to be entered.

The bill alleges that the notes executed by complainant have been transferred to the Commercial National Bank, in payment of a pre-

agreement were to be issued at a gross overvaluation. *Held*, that the agreement was *ultra vires* and illegal, that the parties to the illegal agreement stand *in pari delicto*, and neither can enforce the contract to make such intentionally fictitious payment against the other. See *accord*, *Zelaya Min. Co. v. Meyer* (1890) 8 N. Y. S. 487, 28 N. Y. St. 759 (issue of stock at 30 per cent. less than par).

In *Arkansas &c. Canal Co. v. Farmers' &c. Trust Co.* (1889) 13 Colo. 587, 22 Pac. 954, *held* that stock issued without value and, therefore, "fictitious" within the provisions of the constitution and of a statute of Colorado, has no validity, and that the holders of such stock have no right to bring a stockholders' suit, as they are not stockholders in any legal or equitable sense. And see *Peoria &c. R. Co. v. Thompson* (1882) 103 Ill. 187, 201, as to the meaning of "fictitious."

See also, *Clarke v. Lincoln Lumber Co.* (1884) 59 Wis. 655, 18 N. W. 492; *Pietsch v. Krause* (1903) 116 Wis. 344, 93 N. W. 9.—Eds.

¹ Portions of opinion omitted.—Eds.

existing debt, with notice of the considerations upon which they were executed. This change, the case being heard upon demurrer, together with the fact that the insolvency of the iron company does not appear, justifies us, for the purposes of this case, in treating the bank, as the holder of these stock notes, as standing upon no higher ground than the assignor.

The complainant seeks to be relieved from his subscription upon the ground that the company has refused to carry out its agreement concerning its bonds; that his notes be canceled, and that he have a decree for the money paid in on his subscriptions. He further prays, in the event he be held liable upon his subscription, that the contract by which he was to receive bonds be specifically performed. *Delby-*

The bank and the iron company join in a demurrer, which questions the validity and legality of the contract by which the complainant was to receive the bonds of the company. This demurrer was sustained by the learned Chancellor, and the bill of complainant dismissed.

In considering the meaning and legal effect of the contract set up by the complainant it is important at the outset to observe that this is not the case of a purchase of stock and bonds, or either, in an organized and going corporation. Upon the contrary, the bill states that the contract into which complainant entered was that upon which all shares were to be issued, and that the contract between himself and the corporation constituted what the pleader properly designates the "basis of organization."

* * * * *

The scheme proposed, upon which this corporation was to be organized, fixed the capital stock at \$350,000. The public has a right to presume that this stock has been, in good faith, subscribed, and that it will be paid. They have also the right to presume that the fund thus subscribed and paid in will, in good faith, be retained in the business of the company, and that it, or the plant and property represented by it, will, in good faith, be held and preserved as a capital and basis of credit and confidence. This much is held out to the public by the representation that its capital stock is \$350,000. But running along with this proposition that there shall be a capital stock of \$350,000 is the additional stipulation that the property of the company, which is to be procured by means of this capital stock, is to be mortgaged to secure bonds in amount precisely equal to the whole capital stock, and these bonds, instead of being sold for their market-value, and the proceeds applied to corporate uses, are to be divided out among the stockholders.

Says complainant in his bill: "Every subscriber was to have bonds and also stock of the company, each to the amount of the subscription." The result of this scheme, if it had been carried out, would have been that each subscriber would have received the obligation of the company to repay to him, with interest, his contribution to the capital stock of the company, and this obligation

would have been secured by a first mortgage upon all the company's property.

It was an arrangement whereby the franchise was to be secured, and at the same time deprive the public of the security which by law they are entitled to have, and upon which the grant of the franchise depends. Whatever the real motive and purpose of the promoters of this arrangement may have been, its legal effect, if valid, would have been to have thrown all the risks and hazards of the business upon the public who should deal with it, while the contributors were to reap all possible gains, and should be secured against loss in the event the enterprise proved unprofitable.

Is a contract by which a corporation agrees to repay to the contributors of its capital stock their several contributions, and whereby such contributions are converted into corporate debts, valid even as against the corporation? Upon what consideration does such an agreement rest? and what power has a corporation to bind itself by such a contract?

It is true, creditors out of the way, that the assets of a private business corporation belong, in the last analysis, to the stockholders, and that they may, by consent, cease business, and divide the property among themselves. But this ownership of assets is subject to the higher and superior rights of creditors, and as against them share-holders have no rights in these assets. No consent of the corporation or of its share-holders can effectually defeat the prior and superior claims of creditors to the corporation property. Upon the winding up of such a corporation creditors must first be paid. The surplus belongs to the stockholders, and this the corporation is bound to divide among them. But by this contract the corporation, in effect, binds itself to return the capital stock to the share-holders at a fixed time—that is, when the bonds mature—regardless of the rights of creditors, and without winding up the business. More than this, the charter expressly forbids the payment of any dividend which impairs capital stock; yet, by this arrangement, dividends are to be paid under the guise of interest, regardless of its effect upon the capital stock of the company.

It is no answer to say that the invalidity of such bonds as to creditors saves all their rights, and that therefore the corporation ought to be suffered to make such contract with its share-holders as it pleases. This argument ignores two very plain considerations:

First—the fact that a defense could not be made by creditors against these bonds if they should pass into the hands of innocent purchasers for value.

Second—the public policy of this State, as is evident from its legislation concerning such corporations, forbids the recognition of such an agreement.

The theory upon which the State has rendered the acquirement of the franchise to be a corporation so speedy and inexpensive is based upon the assumption that the capital stock which the company

holds itself out as having will be in fact paid in, and will stand as a basis of credit instead of individual liability of those associated in business. To secure a corporate capital which shall be a just substitute for personal liability, the law requires, in explicit terms, that nothing shall be received in payment of the capital stock of a manufacturing corporation but cash, or bonds or patent rights at a fair and agreed valuation. The charter further prevents the creation of debts beyond the capital stock; it prohibits the lending of money to shareholders or the payment of dividends in excess of actual profits. The plain and obvious meaning of all these requirements, in the light of the substitution of corporate liability in the place of personal liability beyond the amount of stock subscription, implies that the organization stock shall be paid up in full at its par value. The Courts have not hesitated, either in this State or elsewhere, to denounce every stratagem and device by which the payment of stock subscriptions is sought to be avoided.

The facility with which charters are now obtained, the wonderful increase in the number and power of such organizations, the facilities afforded by the assumption of corporate powers and franchises to bad and designing men to carry out evil and fraudulent schemes whereby the public are to suffer, the plainest principles of common honesty and of business integrity demand that these business corporations shall be held to the utmost good faith in this matter of capital stock, and that all such arrangements as that proposed by this "plan of organization" shall be held void and illegal in that it is prohibited by any fair construction of the corporate powers, and in contravention of the plainest and most obvious principles of public policy concerning such companies. (Such a contract, being prohibited by law, is therefore beyond the power of the corporation, and is void as to the company, being ultra vires.)

What we have said as to the construction and legal effect of the subscriptions involved in the case is not intended to apply to sales of, or subscriptions to, the stock of an organized and going corporation, or the sale of the bonds of a going corporation. The necessities of the business of an organized company might demand an increase of capital stock, and if such stock is lawfully issued, it may very well be offered upon special terms. In such case, if the market price was less than par, (it is clear that a purchaser or subscriber for such stock at its market value would, in the absence of fraud, be liable only for his contract price.) So a case might arise where the stock of a going concern was much depreciated, and where its bonds were likewise below par, and there was lawful authority to issue additional stock and bonds. Now, in such case, the real market value of an equal amount of stock and bonds might not exceed, or even equal, the par value of either. In such case, all questions of fraud aside, a purchaser would only be held for his contract price. The case we have been considering is that of the issue of the initiatory or organization stock,—that class of stock

which is to constitute the capital stock upon which the grant of the franchise depends.

* * * * *

The corporation having refused to execute this agreement, requiring it to issue its bonds to the subscribers for stock, and having determined that such a contract was void and illegal—as beyond the power of the corporation—it cannot, therefore, be specifically executed. (This brings us to a consideration of the question as to whether the refusal of the corporation to execute this illegal agreement relieves complainant from his liability as a subscriber to the capital stock of this company.)

His subscription cannot be regarded as one upon a condition precedent. He subscribed not upon condition that, before he should be required to pay, the shares and bonds should be delivered to him. On the contrary, his bill shows that he has already paid \$1,000 upon his liability, and executed his negotiable notes for the remainder, and he states that he was to pay his subscription “as calls” should be made. He clearly contemplated that his subscription should be paid before any bonds were to be issued, for the bonds were to be secured by a mortgage of the company’s plant, and this could not be created, except upon the supposition that the capital stock should be paid in, and then invested in a plant, which was to be mortgaged to secure the bonds. Where a subscription is taken distinctly upon the condition that it is not to be binding until a stipulated thing is done, then such a subscriber does not become a stockholder, and is not entitled to the rights, or charged with the burdens of a stockholder until the condition has been complied with. This Court said, concerning conditional subscriptions:

“The capital of stock companies consists of their stock subscriptions. This is the basis of credit, and an essential to organization. This is a trust fund for the benefit of creditors in case of insolvency. Conditional subscriptions to the stock of corporations are unusual, and often operate to defeat subscribers who become such absolutely and upon the faith that all the stock is equally bound to contribute to the hazards of the enterprise. It misleads creditors, and is the fruitful source of litigation and disaster. Tending to the ensnarement of creditors, and contrary to a sound public policy, conditional subscriptions to corporate shares ought not to be encouraged.” *Railroad v. Parks*, 2 Pickle 560.

In that case the subscription was payable one-fourth when the railway was completed to the county line; remainder in four equal installments as the work progressed through the county, upon the proviso that the company established a depot at Newbern. The company failed before a depot was established at Newbern, and it was insisted that the subscription was thereby avoided. This Court held that the subscription became absolute upon completion of the road to the county line; that the proviso that a depot should be established at Newbern was not a condition precedent, but an inde-

pendent stipulation; that the acts to be done were to be done at different times, and hence were independent stipulations, and the remedy of the subscriber was for a breach of stipulation in his favor. A condition subsequent is thus defined by Mr. Cook in his work on Stockholders:

"A subscription on a condition subsequent contains a contract between the corporation and the subscriber, whereby the corporation agrees to do some act, thereby combining two contracts—one the contract of subscription, the other an ordinary contract of the corporation to perform certain specified acts. The subscription is valid and enforceable, whether the conditions are performed or not. The condition subsequent is the same as a separate collateral contract between the corporation and the subscriber, for breach of which an action for damages is the remedy." Cook on Stockholders, Section 78.

That Dr. Morrow's purpose was to become a share-holder cannot be doubted. The company regarded him as such, and he so regarded himself, for he not only acted as a stockholder, but became a director of the corporation. Says Mr. Morawetz:

"If it appears that the subscriber intended to become a member of the corporation, and as such entitled to vote at meetings and otherwise enjoy the privileges of membership, it is clear that the subscription cannot be deemed a subscription upon condition precedent." 1 Morawetz on Corporations, Sec. 89.

It follows from all that we have said that the stipulations concerning the issuance of bonds to subscribers for capital stock was not a condition precedent to liability upon the subscription. It was nothing more than an independent stipulation, for the breach of which the remedy would be in damages. The failure of the company to carry out this collateral agreement does not defeat liability upon the subscription. This breached covenant or independent contract was, however, illegal and void, whether regarded as a condition precedent or subsequent, and for such breach no action would lie.

It follows, inasmuch as complainant is liable in equity and at law upon his subscription, that there is no equity whatever in his bill, and the decree dismissing it with costs is *affirmed*.⁸

⁸In *Ersfeld v. Exner* (1908) 128 App. Div. (N. Y.) 135, 112 N. Y. S. 561, Hooker, J., speaking for the majority of the court, said: "It is true that section 42 of the Stock Corporation Law (Laws 1892, chap. 688, as amd. by Laws of 1901, chap. 354) provides that no corporation shall issue either stock or bonds except for money, labor done or property actually received for the use and lawful purposes of such corporation, but nothing in the act contained declares that the stock itself is void where it is issued without such consideration, or that the directors issuing the stock, or a vendor of the particular stock, is liable to a subsequent holder thereof for a violation of the provision of the act. If the corporation itself, and incidentally the plaintiff, has suffered by such unauthorized issue, a proper action doubtless lies for the benefit of the whole corporation, but here the plaintiff sues in his individual capacity." The court *held*, two justices dissenting, that the complaint was

DONALD v. AMERICAN SMELTING & REFINING CO.

1900. 62 N. J. Eq. 729, 48 Atl. 771.

THE opinion of the court was delivered by DIXON, J.

The bill in this case was presented by several holders of stock in the American Smelting and Refining Company to enjoin the company and its directors from entering into a contract with M. Guggenheim's Sons for (1) the transfer to the company of the smelting and refining plants, appurtenant property and business of that firm; (2) the payment by the firm to the company, in cash or in working capital, of a sum equal to two-thirds of the company's working capital on January 1st, 1901, said to be about \$6,000,000, and (3) the payment by the firm to the company of the further sum of \$6,066,666.66 in cash; and for the issuance and delivery to the firm by the company of \$45,200,000 in aggregate par value of the company's capital stock, one-half thereof preferred and one-half common; and also to enjoin them from increasing the capital stock of the company from \$65,000,000 to \$100,000,000, in order to use the added \$35,000,000 with \$10,200,000 of its originally authorized capital stock still held by the company for the carrying out of such bargain.

On filing the bill and accompanying affidavits an order to show cause and stay were granted by the chancellor, which, on the coming in of the answer and its accompanying affidavits, were discharged. Thereupon the complainants appealed to this court, and having secured from us a stay pending the appeal, brought on for hearing the application for an injunction *pendente lite*.

The controversy in its present stage turns upon the charge of the complainants, that the cash and property to be acquired by the company are not worth the par value of the stock to be issued therefor, and hence that the transaction contemplated is illegal.

The rule to be applied in determining whether on such a contention a contemplated original issue of corporate stock is legal or not, is prescribed by sections 48 and 49 of our corporation act. P. L. of 1896 p. 277. They run as follows:

"48. Nothing but money shall be considered as payment of any part of the capital stock of any corporation organized under this act, except as hereinafter provided in case of the purchase of property.

"49. Any corporation formed under this act may purchase mines, manufactories or other property necessary for its business or the stock of any company or companies owning, mining, manufacturing or producing materials or other property necessary for its business,

properly dismissed, and that plaintiff could not recover the face value of the shares from his assignor.

See also *Christensen v. Eno* (1887) 106 N. Y. 97, 101, 12 N. E. 648, 60 Am. Rep. 429; *Currie's Case* (1862) 3 De G. J. & T. 367.—Eds.

and issue stock to the amount of the value thereof in payment therefor."

The meaning of section 48 is not questionable. The money must equal the face value of the stock. The language of section 49 is even more explicit. The corporation may issue stock to the amount of the value of the property. The value of the property in the one case, just as the value of the money in the other, must at least equal the face value of the stock. Such was the view expressed for this court by Mr. Justice Depue in *Wetherbee v. Baker*, 8 Stew. Eq. 501, and supported by abundance of authority.

The distinction between the contemplated issue of corporate stock for property and its issue for money lies, not in the rule for valuation, but in the fact that different estimates may be formed of the value of property. When such differences are brought before judicial tribunals, the judgment of those who are by law entrusted with the power of issuing stock "to the amount of the value of the property," and on whom, therefore, is placed the first duty of valuing the property, must be accorded considerable weight. But it cannot be deemed conclusive when duly subjected to judicial scrutiny. Nor is it necessary that conscious overvaluation or any other form of fraudulent conduct on the part of these primary valuers should be shown to justify interposition. Their honest judgment, if reached without due examination into the elements of value, or if based in part upon an estimate of matters which really are not property, or if plainly warped by self-interest, may lead to a violation of this statutory rule as surely as would corrupt motive.

The cases in this state to which we are referred (*Elkins v. Camden and Atlantic Railroad Co.*, 9 Stew. Eq. 241; *Park v. Grant Locomotive Works*, 13 Stew. Eq. 114; *Ellerman v. Chicago Junction Railway Co.*, 4 Dick. Ch. Rep. 217; *Willoughby v. Chicago Junction Railway Co.*, 5 Dick. Ch. Rep. 656; *Sewell v. East Cape May Beach Co.*, 5 Dick. Ch. Rep. 717; *Edison v. Edison United Phonograph Co.*, 7 Dick. Ch. Rep. 620) in support of the proposition that the honest judgment of the managers of a corporation, with respect to matters intra vires, cannot be disturbed at the instance of stockholders; all relate to transactions for which the legislature has set up no other criterion than the discretion of those managers. But the original issue of corporate stock is a special function, in the exercise of which the legislature has fixed the standard to be observed, and it is the duty of the courts, so far as their jurisdiction extends, to see that this standard is not violated, either intentionally or unintentionally.

When corporate stock has once been issued for property purchased, then the legislature has directed the application of a different rule. In the words of the same section 49, "the stock so issued shall be full-paid stock, and not liable to any further call, neither shall the holder thereof be liable for any further payment under the provisions of this act; and in the absence of actual fraud in the

transaction the judgment of the directors as to the value of the property purchased shall be conclusive."

Under these provisions, after the property has been purchased and the stock issued therefor, nothing short of actual fraud in the transaction can impair the right of the holder to hold his stock as full-paid stock, free from further call. The cases of *Bickley v. Schlag*, 1 Dick. Ch. Rep. 533, and *Rural Homestead Co. v. Wildes*, 9 Dick. Ch. Rep. 668, indicate that the completed transaction was equally secure, even before the statute received its present decisive form.

By the rule above stated, then, the matter in hand must be judged.

The evidence before us shows that in the bargain projected M. Guggenheim's Sons were to give, for \$45,200,000 of stock, about \$12,000,000 in cash in working capital, their plants at Perth Amboy, New Jersey; at Pueblo, Colorado; at Aguas Calientes and Monterey, Mexico, and somewhere in South America, and their leases and contracts, the nature of which is not disclosed in these proceedings. Regarding "the cash and working capital" as so much money, and setting it off against an equal amount of stock, there remains about \$33,000,000 of stock to be equivalenced by the property purchased. It is substantially admitted that the value of the plants themselves as physical possessions does not exceed \$10,000,000, thus leaving about \$23,000,000 to be made up in the value of the good-will of the business and the leases and contracts mentioned.

The defendants insist that the complainants have not borne the burden cast upon them by law of proving that these items are not worth that sum, and certainly we would be unwilling now to adjudge that such a negative is established. But it must be remembered that the cause is yet in a preliminary stage; that the complainants have shown the value of everything which they could reasonably be expected to discover before instituting their suit; that the directors are their trustees, and are intending a very large issue of stock for property which they have not seen fit hitherto to define. Under these circumstances, the legal rule imposing the burden of proof on the complainant should not be rigorously applied. Indeed, as these trustees are seeking to exercise a specially delegated power, which can be justly exercised only in accordance with a prescribed standard, it is not entirely clear that a burden does not rest on them, when challenged beforehand, to vindicate their proposed action. But assuming the burden to be on the complainants, we think that for present purposes it is sustained.

The proofs point strongly to the conclusion that in the negotiations between the parties the real value of the property to be acquired has not been the basis on which they have determined the amount of stock to be issued therefor. This is explicitly stated in the affidavit annexed to the answer made by Daniel Guggenheim, who had charge of the negotiations on behalf of his firm. He said:

"From the outset the purpose of both parties was to reach a just conclusion as to comparative values, and to determine on that

basis what amount of the securities we would justly receive for our business and properties as against those of the American company, represented by its outstanding \$54,800,000 of stock." In other words, on the assumption that the possessions of the company are worth \$54,800,000, the parties concluded that what the firm was to deliver to the company is worth \$45,200,000. [This mode of arriving at the value of property to be purchased by the issue of stock is not that contemplated by the statute, and can be made to accord with it only by proof that the assumption is well found.] But there is no support for the assumption above stated, except the general averment that the company's net earnings for the year ending October 31st, 1900, exceed \$4,500,000, i. e., about eight and a half per cent. of the par value of its outstanding stock, and the fact that the shares of that stock are fully paid. The earnings of a single year hardly afford satisfactory evidence of the value of the company's property, and whether the shares are "fully paid" merely because they were issued for property purchased, without the presence of fraud in the transaction, and whether the consideration received for them has depreciated since the company was organized in April, 1899, we have not the means of knowing. What the defendants have taken care to show to the court, though for another purpose, is that the commercial world has never, until the proposed bargain came into view, estimated the stock of the company at more than two-thirds of its face value.

The fact just mentioned underlies another position taken by the defendants viz., that the contemplated contract would be advantageous to the company and its stockholders, since even the mere expectation that it would be consummated has increased the value and market price of the stock, and, therefore, it is argued, the complainants, as stockholders, are not aggrieved. But not there is the pith of the controversy. If the intrinsic value and market price of the company's stock were only sixty per cent. of its face, and an outsider were to offer eighty per cent. in money for additional stock to be issued, such an offer would clearly be advantageous to the company and its stockholders; but it could not be legally accepted, because [the legislature has required that one hundred per cent., whether in cash or in property, shall be received for corporate stock when originally issued.] It is the illegality of the transaction which warrants complaint. Stockholders have the same right to prevent an issue of stock in violation of the statute as they have to prevent a use of corporate property beyond the scope of the corporate power, without regard to loss or gain. Pom. Eq. Jur. §§ 1093, 1095.

In view of the undefined nature of the property for which \$23,000,000 of stock is to be issued, of the illegitimate basis on which the price to be paid for that property appears to have been fixed, and of the probability that the stock has been rated by the parties at its market value rather than at par, we think proper ground is

shown for restraining the completion of the contract until full investigation can be made.

With regard to the mere act of increasing the capital stock, the defendants contend that, as the board of directors and two-thirds of the stockholders have voted in favor of the increase, the court cannot interfere. But evidently this act of the corporate authorities must stand on the same footing as other corporate doings. The fact that in making an increase of stock two-thirds of the stockholders have concurred with the board of directors, does not relieve their action from the rule that corporate bodies must keep within the legislative bounds of their authority, with respect to their ends as well as to their means. They cannot be justified in an attempt to increase the capital stock for an illegitimate object, e. g., to found a charity, or in order to issue the stock for less than par. But if the claim of these complainants shall ultimately prove well founded, this proposed increase has been favored for the purpose of so issuing it, and with no other design. The circular letter sent out by the directors to the stockholders to secure their assent to the increase expressly declared that the object was to effectuate the contemplated bargain with M. Guggenheim's Sons. If the stock can lawfully be used for that purpose, the stockholders have assented to the increase and the complainants must acquiesce, but if it cannot, then it would be utterly inequitable, not only to the complainants, but also to the stockholders who have voted for it, to hold that authority for the increase has been properly given.

The proceedings to increase the stock should likewise remain *in statu quo*.

COLLINS, J. (dissenting).

The affidavits submitted by the complainants were limited to the cost of reproduction of certain smelting and refining works specified and were largely based on common report. No attempt was made to place a value upon all the "smelting and refining plants, appurtenant property and business" of the firm of M. Guggenheim's Sons as a going concern, and there is no charge or proof that information on that subject was ever denied or even asked. The answer filed made all discovery prayed, and there is nothing in that answer or the accompanying affidavits inconsistent with the statutory requirements as to the issue of stock. It does indeed appear that M. Guggenheim's Sons were influenced, in deciding to sell their property for the price agreed on, by a comparison of the values of the two interests, to be in effect consolidated, as applied to the total stock issue that would eventually represent those interests, but it does not follow that actual values are below the face of the stock. The defendants were not, in my opinion, called on to prove anything on the subject, but it does appear from the affidavits they submitted that on the legitimate basis of earning power the stock values are actual values. I attach no importance to the exchange quotations of the stock of the defendant company. The

price-secured for such of the stock of new corporations, especially those of an industrial character, as gets into the general market affords very little indication of real value.

I think the complainants failed to prove, *prima facie*, any charge in their bill, and shall therefore vote to affirm the order denying them an injunction, and I am authorized to say that the other judges so voting concur in this opinion.

For reversal—THE CHIEF-JUSTICE, VAN SYCKEL, DIXON, GARRISON, HENDRICKSON, ADAMS, VREDENBURGH, VOORHEES, VROOM

—9.

For affirmance—GUMMERE, COLLINS, FORT, GARRETSON, BOGERT

—5.*

* In *New Castle Northern R. Co. v. Simpson* (1884) 21 Fed. 533, *held* that a railroad corporation which had entered into a construction contract to issue stock and bonds largely in excess of the cost of construction could maintain a bill in equity to rescind the contract while it was still executory, the maxim *in pari delicto* not applying where the contract is executory, and the stock being illegal and void under the provisions of the Constitution of Pennsylvania to the effect that "no corporation shall issue stocks or bonds except for money, labor done, or money or property actually received; and all fictitious increase of stock or indebtedness shall be void." On page 536, the court says: "For every dollar's worth of labor done for the corporation, or property received by it, or of money expended in its behalf, the defendant is to receive more than threefold in the stock and bonds of the company. A door is thus to be opened for throwing upon the market, to the beguilement of confiding people, corporation securities apparently representing \$600,000 of real value, but having actually behind them \$180,000 of value only. The above-quoted section of the new constitution of the state has strangely mis-carried, if such an issue of 'watered stock' and unsubstantial bonds can be emitted. If the transaction in hand is not within its prohibition, it would be difficult to conceive anything that would be. If the proposed issue of stock and bonds beyond the sum of \$180,000 would not be 'fictitious,' it is hard to divine the meaning which the framers of the constitution attached to that word." *Cf. Memphis & Little Rock R. v. Dow* (1886) 120 U. S. 287, 7 Sup. Ct. 482, 30 L. ed. 595; *Pollitz v. Wabash R. Co.* (1912) 150 App. Div. (N. Y.) 715, 135 N. Y. S. 789, modified on appeal, (1912) 100 N. E. 721.

In *Goodnow v. American Writing Paper Co.* (1907) 72 N. J. Eq. 645, 66 Atl. 607, *aff'd.* (1908) 73 N. J. Eq. 692, 69 Atl. 1014, *held*, "a contract between the company and its stockholders that the stock issued to them is full paid, and not subject to further call, is, in the absence of fraud affecting other shareholders, binding upon the company and its stockholders, although subject to attack by creditors." *Scovill v. Thayer* (1881) 105 U. S. at pp. 153-4; *Wells v. The Green Bay & c. Canal Co.* (1895) 90 Wis. 442, at p. 452, 64 N. W. 69, *Accord.*

See also *Green v. Abietine Medical Co.* (1892) 96 Cal. 322, 31 Pac. 100.

As to the liability of a corporation which has issued watered stock to a forfeiture of its charter, see, *State v. Minn. Thresher Mfg. Co.* (1889) 40 Minn. 213, 41 N. W. 1020, 3 L. R. A. 510; *State ex rel. v. Webb* (1892) 97 Ala. 111, 12 So. 377, 38 Am. St. 151; *State ex rel. v. Janesville Water Power Co.* (1896) 92 Wis. 496, 66 N. W. 512, 32 L. R. A. 391; *Cheetham v. McCormick* (1896) 178 Pa. St. 186, 35 Atl. 631.—Eds.

Section 8.—Stockholders' Right to Sue on Behalf of the Corporation or on Their Own Behalf. Powers of the Majority.

FOSS v. HARBOTTLE.

1843. 2 Hare 461.¹

VICE-CHANCELLOR (Sir James Wigram):—The relief which the bill in this case seeks, as against the Defendants who have demurred, is founded on several alleged grounds of complaint; of these it is only necessary that I should mention two, for the consideration of those two grounds involves the principle upon which I think all the demurrers must be determined. One ground is, that the directors of the Victoria Park Company, the Defendants Harbottle, Adshead, Byrom, and Bealey, have, in their character of directors, purchased their own lands of themselves for the use of the company, and have paid for them, or, rather, taken to themselves out of the monies of the company a price exceeding the value of such lands: the other ground is, that the Defendants have raised money in a manner not authorized by their powers under their act of incorporation; and, especially, that they have mortgaged or encumbered the lands and property of the company, applied the monies thereby raised in effect, circuitously, to pay the price of the land which they had so bought of themselves.

I do not now express any opinion upon the question, whether, leaving out of view the special form in which the Plaintiffs have proceeded in the suit, the bill alleges a case in which a Court of Equity would say that the transactions in question are to be opened or dealt with in the manner which this bill seeks that they should be. * * *

For the present purpose, I shall assume that a case is stated, entitling the company, as matters now stand, to complain of the transactions mentioned in the bill.

The Victoria Park Company is an incorporated body and the conduct with which the Defendants are charged in this suit is an injury not to the Plaintiffs exclusively; it is an injury to the whole corporation by individuals whom the corporation entrusted with powers to be exercised only for the good of the corporation. And from the case of the Attorney-General v. Wilson (1), (without going further), it may be stated as undoubted law, that a bill or information by a corporation will lie to be relieved in respect of injuries which the corporation has suffered at the hands of persons standing in the situation of the directors upon this record. This bill, however, differs from that in the Attorney-General v. Wilson in this,—that instead of the corporation being formally represented as plaintiffs, the bill in this case is brought by two individual corporators,

¹ The statement of facts has been omitted.—Eds.
(1) Cr. & Ph. 1.

professedly on behalf of themselves and all the other members of the corporation, except those who committed the injuries complained of,—the plaintiffs assuming to themselves the right and power in that manner to sue on behalf of and represent the corporation itself.

It was not, nor could it successfully be argued, that it was a matter of course for any individual members of a corporation thus to assume to themselves the right of suing in the name of the corporation: In law, the corporation, and the aggregate members of the corporation, are not the same thing for purposes like this; and the only question can be, whether the facts alleged in this case justify a departure from the rule which prima facie would require that the corporation should sue in its own name and in its corporate character, or in the name of some one whom the law has appointed to be its representative. ?

The demurrers are,—first, of three of the directors of the company, who are also alleged to have sold lands to the corporation under the circumstances charged; secondly, of Bealey, also a director, alleged to have made himself amenable to the jurisdiction of the Court to remedy the alleged injuries, though he was not a seller of land; thirdly, of Denison, a seller of land, in like manner alleged to be implicated in the frauds charged, though he was not a director; fourthly, of Mr. Bunting, the solicitor, and Mr. Lane, the architect of the company. These gentlemen are neither directors nor sellers of land, but all the frauds are alleged to have been committed with their privity, and they also are in this manner sought to be implicated in them. The most convenient course will be, to consider the demurrer of the three against whom the strongest case is stated; and the consideration of that case will apply to the whole.

The first objection taken in the argument for the Defendants was, that the individual members of the corporation cannot in any case sue in the form in which this bill is framed. During the argument I intimated an opinion, to which, upon further consideration, I fully adhere, that the rule was much too broadly stated on the part of the Defendants. [I think there are cases in which a suit might properly be so framed.] Corporations like this, of a private nature, are in truth little more than private partnerships; and in cases which may easily be suggested, it would be too much to hold that a society of private persons associated together in undertakings which, though certainly beneficial to the public, are nevertheless matters of private property, are to be deprived of their civil rights, inter se, because, in order to make their common objects more attainable, the crown or the legislature may have conferred upon them the benefit of a corporate character. If a case should arise of injury to a corporation by some of its members, for which no adequate remedy remained, except that of a suit by individual corporators in their private characters, and asking in such character the protection of those rights to which in their corporate character they were entitled, I cannot but think that the principle so forcibly laid down

by Lord Cottenham in *Wallworth v. Holt* (a), and other cases, would apply, and the claims of justice would be found superior to any difficulties arising out of technical rules respecting the mode in which corporations are required to sue.

But, on the other hand, it must not be without reasons of a very urgent character that established rules of law and practice are to be departed from,—rules, which, though in a sense technical, are founded on general principles of justice and convenience; and the question is, [whether a case is stated in this bill entitling the Plaintiffs to sue in their private characters.] [His Honor stated the substance of the act.] The result of these clauses is, that the directors are made the governing body, subject to the superior control of the proprietors assembled in general meetings; and, as I understand the act, the proprietors so assembled have power, due notice being given of the purposes of the meeting, to originate proceedings for any purpose within the scope of the company's powers, as well as to control the directors in any acts which they may have originated. There may possibly be some exceptions to this proposition, but such is the general effect of the provisions of the statute.

Now, that my opinion upon this may be clearly understood, I will consider separately the two principal grounds of complaint to which I have adverted, with reference to a very marked distinction between them. The first ground of complaint is one which, though it might *prima facie* entitle the corporation to rescind the transactions complained of, does not absolutely and of necessity fall under the description of a void transaction. The corporation might elect to adopt those transactions, and hold the directors bound by them. In other words, the transactions admit of confirmation at the option of the corporation. The second ground of complaint may stand in a different position; I allude to the mortgaging in a manner not authorized by the powers of the act. This, being beyond the powers of the corporation, may admit of no confirmation whilst any one dissenting voice is raised against it. This distinction is found in the case of *Preston v. The Grand Collier Dock Company* (a).

On the first point, it is only necessary to refer to the clauses of the act to show, that, whilst the supreme governing body, the proprietors at a special general meeting assembled, retain the power of exercising the functions conferred upon them by the act of incorporation, it cannot be competent to individual corporators to sue in the manner proposed by the Plaintiffs on the present record. This in effect purports to be a suit by *cestui que trusts*, complaining of a fraud committed or alleged to have been committed by persons in a fiduciary character. The complaint is, that those trustees have sold land to themselves, ostensibly for the benefit of the *cestui que trusts*. The proposition I have advanced is, that although the act should prove to be voidable, the *cestui que trusts* may elect to confirm it.

(2) 4 Myl. & Cr. 635. See also 17 Ves. 320, per Lord Eldon.

(3) 11 Sim. 327; 2 Railway Cases, 335.

Now, who are the cestui que trusts in this case? The corporation, in a sense, is undoubtedly the cestui que trust; but the majority of the proprietors at a special general meeting assembled, independently of any general rules of law upon the subject, by the very terms of the incorporation in the present case, has power to bind the whole body, and every individual corporator must be taken to have come into the corporation upon the terms of being liable to be so bound. How then can this Court act in a suit constituted as this is, if it is to be assumed, for the purposes of the argument, that the powers of the body of the proprietors are still in existence, and may lawfully be exercised for a purpose like that I have suggested? Whilst the Court may be declaring the acts complained of to be void at the suit of the present Plaintiffs, who in fact may be the only proprietors who disapprove of them, the governing body of proprietors may defeat the decree by lawfully resolving upon the confirmation of the very acts which are the subject of the suit. The very fact that the governing body of proprietors assembled at the special general meeting may so bind even a reluctant minority, is decisive to shew that the frame of this suit cannot be sustained whilst that body retains its functions. In order then that this suit may be sustained, it must be shown either that there is no such power as I have supposed remaining in the proprietors, or, at least, that all means have been resorted to and found ineffectual to set that body in motion—this latter point is nowhere suggested in the bill—there is no suggestion that an attempt has been made by any proprietor to set the body of proprietors in motion, or to procure a meeting to be convened for the purpose of revoking the acts complained of. The question then is, whether this bill is so framed as of necessity to exclude the supposition that the supreme body of proprietors is now in a condition to confirm the transactions in question; or, if those transactions are to be impeached in a court of justice, whether the proprietors have not power to set the corporation in motion for the purpose of vindicating its own rights.

* * * * *

The view of the case which has appeared to me conclusive, is, that the existence of a board of directors *de facto* is sufficiently apparent upon the statements in the bill. * * * Whatever the bill may say of the illegal constitution of the board of directors, because the individual directors are not duly qualified, it does not anywhere suggest that there has not been during the whole period, and that there was not when the bill was filed, a board of directors *de facto*, acting in and carrying on the affairs of the corporation, and whose acting must have been acquiesced in by the body of proprietors; at least, ever since the illegal constitution of the board of directors became known, and the acts in question were discovered. But if there has been or is a board *de facto*, their acts may be valid, although the persons so acting may not have been duly qualified. The 114th section of the act provides that "all acts, deeds, and

things, done or executed at any meeting of the directors, by any person acting as a director of the said company, shall, notwithstanding it may afterwards be discovered that there was some defect or error in the appointment of such director, or that such director was disqualified, or, being an interim director, was disapproved of by an annual general meeting of proprietors, be as if such person had been duly appointed and was qualified to be a director." The foundation upon which I consider the Plaintiffs can alone have a right to sue in the form of this bill must wholly fail, if there has been a governing body of directors de facto. There is no longer the impediment to convening a meeting of proprietors, who by their vote might direct proceedings like the present to be taken in the name of the corporation, or of a treasurer of the corporation, (if that were necessary); or who, by rejecting such a proposal, would, in effect, decide that the corporation was not aggrieved by the transactions in question. Now since the 2nd of January, 1840, there must have been three annual general meetings of the company held in July in every year, according to the provisions of the act. These annual general meetings can only be regularly called by the board of directors. The bill does not suggest that the requisitions have not been complied with in this respect, either by omitting to call the meeting, or by calling it informally; but the bill, on the contrary, avers that several general meetings, and extraordinary general meetings, and other meetings of the shareholders of the company, were duly convened and held at divers times between the time when the company was established and the year 1841; including, therefore, in this period of formality of proceeding, as well as of capacity in constitution, an entire year after Westhead's bankruptcy.

Another statement of the bill leading to the same inference,—the existence of an acting board,—is that which avers, that since the year 1839, down, in fact, to the time of filing the bill, that is, during these three years, the company has had no office of its own, but the affairs of the company have been principally conducted at the office of Mr. Bunting. Now this, as I must read it, is a direct admission that the affairs of the company have been carried on by some persons. By whom then have they been carried on? The statute makes the board of directors the body by whom alone those affairs are to be ordered and conducted. There is no other person or set of persons empowered by the act to conduct the affairs of the company; and there is no allegation in the bill that any persons, other than the board of directors originally appointed, have taken upon themselves that business. In the absence of any special allegation to the contrary, I am bound to assume that the affairs of the company have been carried on by the body in whom alone the powers of that purpose were vested by the act, viz., a board of directors.

Again, the bill alleges, that, since the bankruptcy of Westhead, the bankrupts have joined in executing the conveyances of the property of the company to mortgagees. It could only have been in the

character of directors that they could confer any title by the conveyance; in that character the mortgagees would have required them to be parties, and it is in that character that I must assume they executed the deeds.

If the case rested here, I must of necessity assume the existence of a board of directors, and in the absence of any allegation that the board *de facto*, in whose acting the company must, upon this bill, be taken to have acquiesced, have been applied to and have refused to appoint a clerk and treasurer, (if that be necessary), or take such other steps as may be necessary for calling a special general meeting, or had refused to call such special general meeting, the bill does not exclude every case which the pleader was bound to exclude in order to justify a suit on behalf of a corporation, in a form which assumes its practical dissolution. But the bill goes on to shew that special general meetings have been holden since January, 1840. The bill, as I have before observed, states that several general meetings, and extraordinary general meetings, have been holden between the establishment of the company and the year 1841, not excluding the year 1840, which was during Westhead's disqualification,—“and that at such meetings false and delusive statements, respecting the circumstances and prospects of the company, were made by the said directors of the company to the proprietors who attended such meetings, and the truth of the several fraudulent and improper acts and proceedings herein complained of was not disclosed;” and the bill specifies some meetings in particular. Against the pleader, I must intend, that some such meetings may have been holden at a time when there was no board properly constituted, treasurer or principal office of the company, save such as appear by the bill to have existed; and if that were so, the whole of the case of the Plaintiffs, founded on the impracticability of calling a special general meeting, fails. Assuming then, as I am bound to do, the existence, for some time at least, of a state of things in which the company was governed by a board of directors *de facto*, some of the members of which were individually disqualified, and in which, notwithstanding the want of a clerk, treasurer, or office, the powers of the proprietors were called into exercise at general meetings, the question is, when did that state of things cease to exist, so as to justify the extraordinary proceeding of the Plaintiffs by this suit? The Plaintiffs have not stated by their bill any facts to shew that such was not the actual state of things at the time their bill was filed, and, in the absence of any statement to the contrary, I must intend that it was so.

I have applied strictly the rule of making every intendment against the pleader in this case,—that is, of intending every thing to have been lawful and consistent with the constitution of the company, which is not expressly shewn on the bill to have been unlawful or inconsistent with that constitution. And I am bound to make this intendment, not only on the general rule, but also on the rules of

pleading which require a plaintiff to frame his case so distinctly and unambiguously, that the Defendant may not be embarrassed in determining on the form which his defense should assume. *Attorney-General v. Corporation of Norwich* (a). The bill, I cannot but observe, is framed with great care and with more than ordinary professional skill and knowledge; but the averments do not exclude that which, *prima facie*, must be taken to have been the case, that during the years 1840, 1841, and 1842, there was a governing body,—that by such body the business of the company was carried on,—that there was no insurmountable impediment to the exercise of the powers of the proprietors assembled in general meetings to control the affairs of the company, and that such general meetings were actually held. The continued existence of a board *de facto* is not merely not excluded by the averments, but the statements in the bill of the acts which have been done suppose, and even require, the existence of such a board. * * *

The second point which relates to the charges and incumbrances alleged to have been illegally made on the property of the company is open to the reasoning which I have applied to the first point, upon the question whether, in the present case, individual members are at liberty to complain in the form adopted by this bill; for why should this anomalous form of suit be resorted to, if the powers of the corporation may be called into exercise? But this part of the case is of greater difficulty upon the merits. I follow, with entire assent, the opinion expressed by the Vice-Chancellor in *Preston v. The Grand Collier Dock Company*, that, if a transaction be void, and not merely voidable, the corporation cannot confirm it, so as to bind a dissenting minority of its members. But that will not dispose of this question. The case made with regard to these mortgages or incumbrances is, that they were executed in violation of the provisions of the act. The mortgagees are not defendants to the bill, nor does the bill seek to avoid the security itself, if it could be avoided, on which I give no opinion. The bill prays inquiries with a view to proceedings being taken aliunde to set aside these transactions against the mortgagees. The object of this bill against the defendants is to make them individually and personally responsible to the extent of the injury alleged to have been received by the corporation, from the making of the mortgages. Whatever the case might be, if the object of the suit was to rescind these transactions, and the allegations in the bill shewed that justice could not be done to the shareholders without allowing two to sue on behalf of themselves and others, very different considerations arise in a case like the present in which the consequences only of the alleged illegal acts are sought to be visited personally upon the directors. The money forming the consideration for the mortgages was received, and was expended in, or partly in, the transactions which are the subject of the first ground of complaint. Upon this, one question appears to

me to be, whether the company could confirm the former transactions, take the benefit of the money that has been raised, and yet, as against the directors personally, complain of the acts which they have done, by means whereof the company obtains that benefit which I suppose to have been admitted and adopted by such confirmation. I think it would not be open to the company to do this; and my opinion already expressed on the first point is, that the transactions which constitute the first ground of complaint may possibly be beneficial to the company, and may be so regarded by the proprietors, and admit of confirmation. I am of opinion that this question,—the question of confirmation or avoidance,—cannot properly be litigated upon this record, regard being had to the existing state and powers of the corporation, and that therefore that part of the bill which seeks to visit the directors personally with the consequences of the inpeached mortgages and charges, the benefit of which the company enjoys, is in the same predicament as that which relates to the other subject of complaint. Both questions stand on the same ground, and, for the reasons which I stated in considering the former point, these demurrers must be allowed.²

HAWES v. OAKLAND.

1881. 104 U. S. 450, 26 L. ed. 827.³

MR. JUSTICE MILLER delivered the opinion of the court.

This is an appeal from a decree in chancery dismissing the complainant's bill, wherein he, a citizen of New York, alleges that he is a stockholder in the Contra Costa Water-works Company, a California corporation, and that he files it on behalf of himself and all other stockholders who may choose to come in and contribute to the costs and expenses of the suit.

The defendants are the city of Oakland, the Contra Costa Water-works Company, and Anthony Chabot, Henry Pierce, Andrew J. Pope, Charles Holbrook, and John W. Coleman, trustees and directors of the company.

The foundation of the complaint is that the city of Oakland claims at the hands of the company water, without compensation, for all municipal purposes whatever, including watering the streets, public squares and parks, flushing sewers, and the like, whereas it is only entitled to receive water free of charge in cases of fire or

² See *Mozley v. Alston* (1847) 1 Ph. 790. Cf. *Bagshaw v. Eastern &c. R. Co.* (1849) 7 Hare 114, 129 (transaction complained of beyond ratifying power of the majority); *MacDougall v. Gardiner* (1875) L. R. 1 Ch. Div. 13, 25; *Alexander v. Automatic Tel. Co. L. R.* (1900) 2 Ch. Div. 56, 69, rev'g., (1899) 2 Ch. Div. 302. *Contra*, *Gregory v. Patchett* (1864) 33 Beav. 595 (plaintiff need not apply to stockholders' meeting).—Eds.

³ Portion of opinion omitted.—Eds.

other great necessity; that the company comply with this demand, to the great loss and injury of the company, to the diminution of the dividends which should come to him and other stockholders, and to the decrease in the value of their stock. The allegation of his attempt to get the directors to correct this evil will be given in the language of the bill.

He says that "on the tenth day of July, 1878, he applied to the president and board of directors or trustees of said water company, and requested them to desist from their illegal and improper practices aforesaid, and to limit the supply of water free of charge to said city to cases of fire or other great necessity, and that said board should take immediate proceedings to prevent said city from taking water from the works of said company for any other purpose without compensation; but said board of directors and trustees have wholly declined to take any proceedings whatever in the premises, and threatened to go on and furnish water to the extent of said company's means to said city of Oakland free of charge, for all municipal purposes as has heretofore been done, and in cases other than cases of fire or other great necessity, except as for family uses hereinbefore referred to; and your orator avers that by reason of the premises said water company and your orator and the other stockholders thereof have suffered, and will, by a continuance of said acts, hereafter suffer, great loss and damage."

To this bill the water-works company and the directors failed to make answer; and the city of Oakland filed a demurrer, which was sustained by the court and the bill dismissed. The complainant appealed.

Two grounds of demurrer were set out and relied on in the court below, and are urged upon us on this appeal. They are:—

1. That appellant has shown no capacity in himself to maintain this suit, the injury, if any exists, being to the interests of the corporation, and the right to sue belonging solely to that body.

2. That by a sound construction of the law under which the company is organized the city of Oakland is entitled to receive, free of compensation, all the water which the bill charges it with so using.

The first of these causes of demurrer presents a matter of very great interest, and of growing importance in the courts of the United States.

Since the decision of this court in *Dodge v. Woolsey* (18 How. 331), the principles of which have received more than once the approval of this court, the frequency with which the most ordinary and usual chancery remedies are sought in the Federal courts by a single stockholder of a corporation who possesses the requisite citizenship, in cases where the corporation whose rights are to be enforced cannot sue in those courts, seems to justify a consideration of the grounds on which that case was decided, and of the just limitations of the exercise of those principles.

This practice has grown until the corporations created by the laws

of the States bring a large part of their controversies with their neighbors and fellow-citizens into the courts of the United States for adjudication, instead of resorting to the State courts, which are their natural, their lawful, and their appropriate forum. It is not difficult to see how this has come to pass. [A corporation having such a controversy, which it is foreseen must end in litigation, and preferring for any reason whatever that this litigation shall take place in a Federal court, in which it can neither sue its real antagonist nor be sued by it, has recourse to a holder of one of its shares, who is a citizen of another State. This stockholder is called into consultation, and is told that his corporation has rights which the directors refuse to enforce or to protect. He instantly demands of them to do their duty in this regard, which of course they fail or refuse to do, and thereupon he discovers that he has two causes of action entitling him to equitable relief in a court of chancery; namely, one against his own company, of which he is a corporator, for refusing to do what he has requested them to do; and the other against the party which contests the matter in controversy with that corporation. These two causes of action he combines in an equity suit in the Circuit Court of the United States, because he is a citizen of a different State, though the real parties to the controversy could have no standing in that court. If no non-resident stockholder exists, a transfer of a few shares is made to some citizen of another State, who then brings the suit. The real defendant in this action may be quite as willing to have the case tried in the Federal court as the corporation and its stockholder. If so, he makes no objection, and the case proceeds to a hearing. Or he may file his answer denying the special grounds set up in the bill as a reason for the stockholder's interference, at the same time that he answers to the merits. In either event the whole case is prepared for a hearing on the merits, the right of the stockholder to a standing in equity receives but little attention, and the overburdened courts of the United States have this additional important litigation imposed upon them by a simulated and conventional arrangement, unauthorized by the facts of the case or by the sound principles of equity jurisdiction.]

That the vast and increasing proportion of the active business of modern life which is done by corporations should call into exercise the beneficent powers and flexible methods of courts of equity, is neither to be wondered at nor regretted; and this is especially true of controversies growing out of the relations between the stockholder and the corporation of which he is a member. The exercise of this power in protecting the stockholder against the frauds of the governing body of directors or trustees, and in preventing their exercise, in the name of the corporation, of powers which are outside of their charters or articles of association, has been frequent, and is most beneficial, and is undisputed. These are real contests, however, between the stockholder and the corporation of which he is a member.

The case before us goes beyond this.

This corporation, like others, is created a body politic; and corporate, that it may in its corporate name transact all the business which its charter or other organic act authorizes it to do.

Such corporations may be common carriers, bankers, insurers, merchants, and may make contracts, commit torts, and incur liabilities, and may sue or be sued in their corporate name in regard to all of these transactions. The parties who deal with them understand this, and that they are dealing with a body which has these rights and is subject to these obligations, and they do not deal with or count upon a liability to the stockholder whom they do not know and with whom they have no privity of contract or other relation.

The principle involved in the case of *Dodge v. Woolsey* permits the stockholder in one of these corporations to step in between that corporation and the party with whom it has been dealing and institute and control a suit in which the rights involved are those of the corporation, and the controversy is one really between that corporation and the other party, each being entirely capable of asserting its own rights.

This is a very different affair from a controversy between the shareholder of a corporation and that corporation itself, or its managing directors or trustees, or the other shareholder, who may be violating his rights or destroying the property in which he has an interest. Into such a contest the outsider, dealing with the corporation through its managing agents in a matter within their authority, cannot be dragged, except where it is necessary to prevent an absolute failure of justice in cases which have been recognized as exceptional in their character and calling for the extraordinary powers of a court of equity. It is, therefore, always a question of equitable jurisprudence, and as such has, within the last forty years, received the repeated consideration of the highest courts of England and of this country.

(The learned justice proceeded to consider *Foss v. Harbottle*, 2 Hare 461, and *Mozley v. Alston*, 1 Ph. 790.)

These cases have been referred to again and again in the English courts as leading cases on the subject to which they relate, and always with approval.

In *Gray v. Lewis*, decided in 1873, Sir W. M. James, L. J., said: "I am of opinion that the only person, if you may call it a person, having a right to complain was the incorporated society called Charles Lafitte & Co. In its corporate character it was liable to be sued and was entitled to sue; and if the company sued in its corporate character, the defendant might allege a release or a compromise by the company in its corporate character,—a defence which would not be open in a suit where a plaintiff is suing on behalf of himself and other shareholders. I think it is of the utmost importance to maintain the rule laid down in *Mozley v. Alston* and *Foss v. Harbottle*, to which, as I understand, the only exception is where the cor-

porate body has got into the hands of directors, and of the majority, which directors and majority are using their power for the purpose of doing something fraudulent against the minority, who are overpowered by them, as in *Atwood v. Merryweather*, where Vice-Chancellor Wood sustained a bill by a shareholder on behalf of himself and others, and there it was after an attempt had been made to obtain proper authority from the corporate body itself in a public meeting assembled." Law Rep. 8 Ch. App. 1035.

But perhaps the best assertion of the rule and of the exceptions to it are found in the opinion of the court by the same learned justice in *McDougall v. Gardiner*, in 1875, 1 Ch. D. 13. "I am of opinion," he says, "that this demurrer ought to be allowed. I think it is of the utmost importance in all these controversies that the rule which is well known in this court as the rule in *Mozley v. Alston*, and *Lord v. Copper Miner's Company*, and *Foss v. Harbottle*, should always be adhered to; that is to say, that nothing connected with internal disputes between shareholders is to be made the subject of a bill by some one shareholder on behalf of himself and others, unless there be something illegal, oppressive, or fraudulent; unless there is something ultra vires on the part of the company qua company, or on the part of the majority of the company, so that they are not fit persons to determine it, but that every litigation must be in the name of the company, if the company really desire it. Because there may be a great many wrongs committed in a company,—there may be claims against directors; there may be claims against officers; there may be claims against debtors; there may be a variety of things which a company may well be entitled to complain of, but which, as a matter of good sense, they do not think it right to make the subject of litigation; and it is the company, as a company, which has to determine whether it will make anything that is a wrong to the company a subject-matter of litigation, or whether it will take steps to prevent the wrong from being done."

The cases in the English courts are numerous, but the foregoing citations give the spirit of them correctly.

In this country the cases outside of the Federal courts are not numerous, and while they admit the right of a stockholder to sue in cases where the corporation is the proper party to bring the suit, they limit this right to cases where the directors are guilty of a fraud or a breach of trust, or are proceeding ultra vires. *Marsh v. Eastern Railroad Co.*, 40 N. H. 548; *Peabody v. Flint*, 6 Allen (Mass.) 52. In *Brewer v. Boston Theater* (104 Mass. 378), the general doctrine and its limitations are very well stated. See also *Hersey v. Veazie*, 24 Me. 9; and *Samuel v. Holladay*, 1 Woolw. 400.

The case of *Dodge v. Woolsey*, decided in this court in 1855, is, however, the leading case on the subject in this country.

And we do not believe, notwithstanding some expressions in the opinion, that it is justly chargeable with the abuses we have mentioned. It was manifestly well considered, and the opinion is unus-

ually long, discussing the point now under consideration with a full reference to the decisions then made in the courts of England. The suit—a bill in chancery—was brought in the Circuit Court for the District of Ohio, by Woolsey, a stockholder of the Commercial Bank of Cleveland, and a citizen of Connecticut, against that bank, its managing directors, and Dodge, tax-collector of the county in which the bank was situated, citizens of Ohio. The bill alleged that Dodge had levied upon property of the bank to make collection of a tax, which, by the Constitution of the State of Ohio, the bank was bound to pay; that in that respect the Constitution, then recently adopted, impaired the obligation of the contract of the State with the bank, contained in its charter. It appeared in the case that Woolsey had, by letter directed to the board of directors, requested them to institute proceedings to prevent the collection of this tax; but the board, by a resolution, declined to take any such action, while expressing their opinion that the tax was illegal. In the opinion of the court, reciting the circumstances which justified its interposition at the suit of the stockholder, the allegation of the bill is adverted to, that if the taxes are enforced it will annul the contract with the State concerning taxation, and that the *tax is so onerous upon the bank that it will compel a suspension and final cessation of its business*. The following extract from Angell & Ames on Corporations is cited with approval: "Though the result of the authorities clearly is that in a corporation, when acting within the scope of, and in obedience to, the provisions of its constitution, the will of the majority, clearly expressed, must govern, yet beyond the limits of the act of incorporation the will of the majority cannot make the act valid, and the power of a court of equity may be put in motion at the instance of a single shareholder, if he can show that the corporation are employing their statutory powers for the accomplishment of purposes not within the scope of their institution. Yet it is to be observed that there is an important distinction between this class of cases and those in which there is no breach of trust, but only error and misapprehension or simple negligence on the part of the directors." And the court adds: "It is obvious from this rule that the circumstances of each case must determine the jurisdiction of a court of equity to give the relief sought."

A very large part of the opinion is devoted to the consideration of the high function of this court in construing the Constitution of the United States, and it is impossible not to see the influence on the mind of the writer of that opinion of the fact that the only question on the merits of the case was one which peculiarly belonged to the Federal judiciary, and especially to this court to decide; namely, whether the Constitution of the State of Ohio violated the obligation of the contract concerning taxation found in the charter of the bank.

As the law then stood there was no means by which the bank, being a citizen of the same State with Dodge, the tax-collector, could bring into a court of the United States the right which it asserted

under the Constitution, to be relieved of the tax in question, except by writ of error to a State court from the Supreme Court of the United States.

That difficulty no longer exists, for by the act of March 3, 1875, c. 137 (18 Stat., pt. 3, p. 470), all suits arising under the Constitution or laws of the United States may be brought originally in the Circuit Courts of the United States without regard to the citizenship of the parties. Under this statute, if it had then existed, the bank, in *Dodge v. Woolsey*, could undoubtedly have brought suit to restrain the collection of the tax in its own name, without resort to one of its shareholders for that purpose.

And this same statute, while enlarging the jurisdiction of the Circuit Courts in cases fairly within the constitutional grant of power to the Federal judiciary, strikes a blow, by its fifth section, at improper and collusive attempts to impose upon those courts the cognizance of cases not justly belonging to them. It declares, if at any time in the progress of a case, either originally commenced in a Circuit Court, or removed there from a State court, it shall appear to said court "that such suit does not really and substantially involve a dispute or controversy properly within the jurisdiction of said Circuit Court, or that the parties to said suit have been improperly or collusively made or joined, either as plaintiffs or defendants, for the purpose of creating a case cognizable or removable under this act, the said Circuit Court shall proceed no further, but shall dismiss the suit or remand it to the court from which it was removed."

It is believed that a rigid enforcement of this statute by the Circuit Courts would relieve them of many cases which have no proper place on their dockets.

This examination of *Dodge v. Woolsey* satisfies us that it does not establish, nor was it intended to establish, a doctrine on this subject different in any material respect from that found in the cases in the English and in other American courts, and that the recent legislation of Congress referred to leaves no reason for any expansion of the rule in that case beyond its fair interpretation.

We understand that doctrine to be that to enable a stockholder in a corporation to sustain in a court of equity in his own name, a suit founded on a right of action existing in the corporation itself, and in which the corporation itself is the appropriate plaintiff, there must exist as the foundation of the suit—

Some action or threatened action of the managing board of directors or trustees of the corporation which is beyond the authority conferred on them by their charter or other source of organization; ①

Or such a fraudulent transaction completed or contemplated by the acting managers, in connection with some other party, or among themselves, or with other shareholders as will result in serious injury to the corporation, or to the interests of the other shareholders; ②

(3) Or where the board of directors, or a majority of them, are acting for their own interest, in a manner destructive of the corporation itself, or of the rights of the other shareholders;

4 Or where the majority of shareholders themselves are oppressively and illegally pursuing a course in the name of the corporation, which is in violation of the rights of the other shareholders, and which can only be restrained by the aid of a court of equity.

Possibly other cases may arise in which, to prevent irremediable injury, or a total failure of justice, the court would be justified in exercising its powers, but the foregoing may be regarded as an outline of the principles which govern this class of cases.

But, in addition to the existence of grievances which call for this kind of relief, it is equally important that before the shareholder is permitted in his own name to institute and conduct a litigation which usually belongs to the corporation, he should show to the satisfaction of the court that he has exhausted all the means within his reach to obtain, within the corporation itself, the redress of his grievances, or action in conformity to his wishes. He must make an earnest, not a simulated effort, with the managing body of the corporation, to induce remedial action on their part, and this must be made apparent to the court. If time permits or has permitted, he must show, if he fails with the directors, that he has made an honest effort to obtain action by the stockholders as a body, in the matter of which he complains. And he must show a case, if this is not done, where it could not be done, or it was not reasonable to require it.

*must do
3 things
before bringing
action in
his own
name;*

The efforts to induce such action as complainant desires on the part of the directors, and of the shareholders when that is necessary, and the cause of failure in these efforts should be stated with particularity, and an allegation that complainant was a shareholder at the time of the transactions of which he complains, or that his shares have devolved on him since by operation of law, and that the suit is not a collusive one to confer on a court of the United States jurisdiction in a case of which it could otherwise have no cognizance, should be in the bill, which should be verified by affidavit.

It is needless to say that appellant's bill presents no such case as we have here supposed to be necessary to the jurisdiction of the court.

He merely avers that he requested the president and directors to desist from furnishing water free of expense to the city, except in case of fire or other great necessity, and that they declined to do as he requested. No correspondence on the subject is given; no reason for declining. We have here no allegation of a meeting of the directors, in which the matter was formally laid before them for action. No attempt to consult the other shareholders to ascertain their opinions, or to obtain their action. But within five days after his application to the directors this bill is filed. There is no allegation

of fraud or of acts ultra vires, or of destruction of property, or of irremediable injury of any kind.

Conceding appellant's construction of the company's charter to be correct, there is nothing which forbids the corporation from dealing with the city in the manner it has done. That city conferred on the company valuable rights by special ordinance; namely, the use of the streets for laying its pipes, and the privilege of furnishing water to the whole population. It may be the exercise of the highest wisdom to let the city use the water in the manner complained of. The directors are better able to act understandingly on this subject than a stockholder residing in New York. The great body of the stockholders residing in Oakland or other places in California may take this view of it, and be content to abide by the action of their directors.

If this be so, is a bitter litigation with the city to be conducted by one stockholder for the corporation and all other stockholders, because the amount of his dividends is diminished?

This question answers itself, and without considering the other point raised by the demurrer, we are of opinion that it was properly sustained, and the bill dismissed, because the appellant shows no standing in a court of equity—no right in himself to prosecute this suit.

*Decree affirmed.*⁴

ROGERS v. NASHVILLE ETC. R. CO.

1899. 91 Fed. 299, 33 C. C. A. 517.⁵

APPEAL from the Circuit Court of the United States for the Middle District of Tennessee.

This is a bill filed by a stockholder of the Nashville, Chattanooga & St. Louis R. Co., in behalf of himself and all other stockholders in

⁴ Following the decision in the principal case, the Supreme Court of the United States, on Jan. 23, 1882, promulgated Equity Rule No. 94, (see Preface, IX, of 104 U. S.) which constitutes the basis of Equity Rule No. 27, promulgated on Nov. 4, 1912, viz.—

"27.—*Stockholder's Bill.*—Every bill brought by one or more stockholders in a corporation against the corporation and other parties, founded on rights which may properly be asserted by the corporation, must be verified by oath, and must contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share had devolved on him since by operation of law, and that the suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance. It must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action, or the reasons for not making such effort."

See also *Detroit v. Dean* (1882) 106 U. S. 537, 27 L. ed. 300, 1 Sup. Ct. 560 (approving the principal case); *Corbus v. Alaska &c. Min. Co.* (1902) 187 U. S. 455, 23 Sup. Ct. 157, 47 L. ed. 256; *Delaware & Hudson Co. v. Albany &c. R. Co.* (1909) 213 U. S. 435, 29 Sup. Ct. 540, 53 L. ed. 862.—Eds.

⁵ Statement abridged and portions of opinion omitted.—Eds.

said company who may desire to become parties complainant, against the said company and the Louisville & Nashville R. Co., to obtain the cancellation of a lease entered into between the two corporations, whereby the latter company leased to the former, for a term of 99 years, two lines of railroad running from Paducah, Ky., to Memphis, Tenn. Separate demurrers were filed by each of the defendant companies, which were sustained below, and the bill dismissed.

Before TAFT and LURTON, Circuit Judges, and SEVERENS, District Judge.

LURTON, Circuit Judge, after making the foregoing statement of facts, delivered the opinion of the court.

The relief sought is the cancellation of the lease entered into between the Nashville, Chattanooga & St. Louis Railway Company and the Louisville & Nashville Railroad Company. This relief is asked upon several grounds: First, because the contract was fraudulently imposed upon the Nashville, Chattanooga & St. Louis Railway Company by the Louisville & Nashville Railroad Company through its controlling influence as a majority shareholder; second, because the contract is ultra vires, one or both companies; and, third, because, if neither void as ultra vires, nor voidable for fraud, it is such a contract as cannot be legally consummated without ratification by a three-fourths vote of the shareholders. Ratification by a three-fourths vote has never been had, and it is charged that more than one-fourth of the shares are opposed to the lease, and that, though two shareholders' meetings have been held since the making of the lease, action in regard thereto was prevented through adjournments carried by the voting power of the shares held by the lessor company. To this bill the defendants severally demurred. These demurrers go both to the form of the bill and to the merits.

* * * * *

First, as to the form of the bill. The contract of which complaint is made is an injury to all the members of that corporation, and not one to complainant exclusively. The complaint is, that a majority of the directors, to whom is intrusted the exercise of corporate powers for the corporate good exclusively, have betrayed this trust by exceeding the corporate powers, and by entering into an agreement with a majority shareholder very detrimental to the true and exclusive interests of the corporation they represent. The suit is, therefore, one founded upon alleged wrongs which the corporation itself should properly represent. [The general rule is that a corporation shall sue in its corporate character and name.] To justify a departure from this rule by entertaining a suit by an individual member for an injury founded upon a corporate wrong, reasons of a most urgent character must be shown. The essential averments of such a bill by a stockholder were elaborately considered in *Hawes v. Oakland*, 104 U. S. 450, and the practice there declared was subsequently formulated into a rule, and promulgated as equity rule No. 94. The principal matter considered in *Hawes v. Oakland*:

was that of collusive suits, wherein, through a simulated unwillingness of the corporation to bring the suit in its own name and character, jurisdiction was given to a federal court through a suit by a shareholder whose citizenship was such as to give jurisdiction. So far as rule No. 94 deals with the subject of collusive jurisdiction, its requirements are new, and should be closely observed. So far as it deals with the general form of such bills, it prescribes no other or different practice than that commonly imposed by courts of equity. This is evident from the reasoning and conclusions in *Hawes v. Oakland*. [This bill is unobjectionable in form, so far as the rule relates to the matter of collusive jurisdiction.] It is stated that the complainant was a shareholder at the time of the transaction complained of, and is a shareholder now, and that the suit is not a collusive one to confer jurisdiction on a court of the United States in respect to a matter of which it would not otherwise have cognizance, and is properly verified by the oath of the complainant. The objection urged is in respect to the other requirement of the rule that such a bill "shall set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action." The averments of the bill touching the attitude of this complainant towards this lease leave no room to doubt his constant, consistent, and well-understood opposition. What he did to prevent its consummation has been sufficiently stated in stating the case, and need not be repeated. It is not averred that before doing so he requested the directors to bring and conduct this suit. Upon the contrary, it is stated that, having exhausted all known means of defeating the lease within the corporation, he brought this suit, without demanding that the directors should themselves direct and conduct it, upon the ground that such a demand under the facts and circumstances stated in the bill would be idle and nugatory. Undoubtedly, the general rule is that such a bill should contain an averment that a demand was made upon the corporate agents to bring the suit, and that it had been refused or neglected. *Memphis City v. Dean*, 8 Wall. 73; *Cook, Stock, Stockh. & Corp. Law*, § 240. But there are well-settled exceptions to this general rule. The circumstances may be such that the demand would be an idle form, or the suit of such character that it could not be decently brought or managed by those controlling the corporation. A demand and refusal furnish the best evidence that the corporation is unable to protect the rights of its members; but, if the facts are such as to show that such a demand be an idle ceremony, or the action required be such as that the guilty agents of the corporation ought not to be intrusted with the conduct of the necessary suit, none need be made. * * *

Aside from all questions of ultra vires, one ground for relief stated in the bill is that the lessor company through the voting power of the majority of shares owned by it, has elected a majority of the direct-

ors of the lessee company, and, through its influence with that majority, has imposed upon the lessee company a contract with itself, which is oppressive and prejudicial to the general interests of the members of the dominated corporation, and beneficial only to the controlling lessor company. That a majority of the managing officers of the Nashville, Chattanooga & St. Louis Railway Company may have made a bad bargain through misjudgment as to the value of such a lease would be wholly insufficient of itself to justify a court of equity in setting the contract aside at the instance of a dissenting minority. The wisdom or foolishness of such a contract is wholly a question of internal management, to be corrected within the corporation. But this bill charges that this oppressive and prejudicial contract has resulted from the nonexercise of honest judgment by those intrusted with corporate management, and that it has been brought about through the improper and illegal influence of the lessor as dominating stockholder. Thus the gravamen of this ground for relief is fraud, simple fraud. Now, if such a fraud be sufficiently charged, it must be clear that any request to the directors guilty of such an abuse of corporate trust, or interested in supporting the lease so made through interest in the lessor company, would be an idle ceremony,—more than that. Such a suit could not be decently managed and controlled by those whose conduct and motives would be necessarily brought in question. Under such circumstances the act is incapable of confirmation by a majority, and a suit will be entertained by a minority of shareholders in behalf of themselves and all other shareholders, the corporation and offending shareholders being defendants, to set aside such contract, and restore the status quo. When the bill shows that such a fraud has been committed by one who commands a majority of votes in the managing board and in a stockholders' meeting, a member may sue without making a demand upon the managing directors to institute proceedings to undo that which they themselves have done or approved. The reason is plain. If a minority shareholder might not have a remedy under such circumstances, the majority could defraud the corporation, and ruin the minority, with absolute impunity. This question came before the United States court of appeals for the Second circuit in *De Neufville v. Railroad Co.*, 51 U. S. App. 374, 26 C. C. A. 306, 81 Fed. 10, where a bill was filed by a stockholder, as in this case, and for the purpose of asserting the rights of the corporation against the title of a dominating stockholder who had acquired the controlled railroad under a foreclosure sale. The bill was demurred to for non-compliance with rule No. 94. This ground of demurrer was overruled, the court saying:

"There is no force to the suggestion that the bill is defective in failing to 'set forth with particularity the efforts of the plaintiff to secure such action as he desired on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action.' In view of the averments that

defendants obtained control of a majority of the stock and bonds on purpose to wreck the New York & Northern; procured, by resignation and election, a board of directors in harmony with that purpose, and which board did in fact, by refusing profitable business and diverting traffic, accomplish such purpose,—it would be an idle waste of time to urge the board of directors, or the majority stockholders who initiated and consummated the fraud, to bring suit in order to secure judicial condemnation of their own actions.”

* * * * *

In *Atwool v. Merryweather*, L. R. 5 Eq. 464, note, a bill was sustained by members of a corporation against the corporation and two of the directors, and without any request to sue, upon the ground that a majority of the shares were under the control of the parties charged with the fraud against the corporation. It appeared in that case that the transaction complained of was a simple fraud upon the corporation, and was not an ultra vires act, and that at a stockholders' meeting a majority of shares voted to ratify the contract. It appeared, however, that the shares of the beneficiaries in the fraud were voted in favor of ratification, and that without these shares the majority was the other way. The doctrine of *Foss v. Harbottle*, 2 Hare 461, was supposed to prevent the filing of a bill by members of a corporation to set aside a contract which was not ultra vires, and might be, therefore, ratified by the members. To this Vice Chancellor Sir W. Page Wood, said:

“If I were to hold that no bill could be filed by shareholders to get rid of the transaction on the ground of the doctrine of *Foss v. Harbottle*, it would be simply impossible to set aside a fraud committed by a director under such circumstances, as the director obtaining so many shares by fraud would always be able to outvote everybody else.”

In *Menier v. Telegraph Works*, 9 Ch. App. 350, a bill was filed by a shareholder in behalf of himself and all other shareholders against the European Company, in which he was a shareholder, Hooper's Telegraph Works, another corporation, and two of the directors of his own company, for the purpose of preventing the carrying out of a resolution for the winding up of the European Company, and for the abandonment of a pending suit involving the ownership of a valuable concession claimed to have been granted to one Baron de Mana in trust for the European Company. It was charged that these resolutions were adopted “through the influence of Hooper's Company and by the vote of directors elected by the shares owned by Hooper's Company in the European Company, said company owning an absolute majority.” It was also charged that the abandonment of the pending suit and the resolution to wind up were prejudicial to the interests of the European Company and to the advantage of Hooper's Company, and to enable Hooper's Company to accomplish purposes of its own. The bill was demurred to upon the ground that it should be filed in the name of the European Company. There was

no averment that the managing directors of the European Company had been applied to to bring the suit. The demurrer was overruled. Upon appeal this ruling was sustained. Sir W. M. James, said:

"I am of opinion that the order of the vice-chancellor in this case is quite right. The case made by the bill is, very shortly, this: The defendants, who have a majority of shares in the company, have made an arrangement by which they have dealt with matters affecting the whole company, the interest in which belongs to the minority, as well as to the majority. They have dealt with them in consideration of their obtaining for themselves certain advantages. Hooper's Company have obtained certain advantages by dealing with something which was the property of the whole company. The minority of the shareholders say, in effect, that the majority has divided the assets of the company, more or less, between themselves, to the exclusion of the minority. I think it would be a shocking thing if that could be done, because, if so, the majority might divide the whole assets of the company, and pass a resolution that everything must be given to them, and that the minority should have nothing to do with it. Assuming the case to be as alleged in the bill, then the majority have put something into their pockets at the expense of the minority. If so, it appears to me that the minority have a right to have their share of the benefits ascertained for them in the best way which the court can do it, and given to them. It is said, however, that this is not the right form of suit, because, according to the principles laid down in *Foss v. Harbottle*, 2 Hare 461, and other similar cases, the court ought to be very slow, indeed, in allowing a shareholder to file a bill, where the company is the proper plaintiff. This particular case seems to me precisely one of the exceptions referred to by the Vice-Chancellor Wood in *Atwood v. Merryweather*, L. R. 5 Eq. 464, note, a case in which the majority were the defendants, the wrongdoers, who were alleged to have put the minority's property into their pockets. In this case it is right and proper for a bill to be filed by one shareholder on behalf of himself and all other shareholders."

Mason v. Harris, 11 Ch. Div. 97, was a case of much the same character. The bill was filed by a minority of shareholders against three of the directors, being a majority, and the corporation, for the purpose of setting aside, for fraud, a sale made to the corporation by one of the directors. The bill alleged that the selling director and the other two made defendants constituted a majority, and that those two were under the control and influence of the selling director, who owned a majority of the shares in the company, and against whom no step could be taken within the company to remedy the wrong. It was held that the bill would lie, and that the acts were such that no majority of stockholders could sanction as to bind the minority, and that the allegations were such as to make it clear that it was impossible to get the company to impeach them. Jessel, M. R., said:

("As a general rule, the company must sue in respect of a claim of

this nature, but general rules have their exceptions, and one exception to the rule requiring the company to be plaintiff is that, where a fraud is committed by persons who can command a majority of votes, the minority can sue. The reason is plain, as, unless such an exception were allowed it would be in the power of the majority to defraud the minority with impunity. * * * It appears that Harris (the selling director) has obtained such influence over the directors that a majority side with him, and will not do anything to remedy the wrong complained of. It further appears that Harris holds such a number of shares that he can outvote those who wish the sale set aside. By reason, therefore, of his influence with the directors and his number of votes, he has the sole control of the company. The case is precisely within the rule laid down by Lord Justice James in *Menier v. Telegraph Works*, 9 Ch. App. 350. Is it reasonable to say to a minority of shareholders who are defrauded by the majority that they must apply to the company to institute proceedings? Even independently of the authorities, I should be prepared to say 'No.' Facts are alleged which show it to be impossible to get the company to impeach the acts complained of."

The case of *Transportation Co. v. Beatty*, 12 App. Cas. 589, is not in conflict with the cases cited. The claim in the suit was to set aside a sale made to the company by Beatty, who was a director, of a steamer of which he was sole owner. A by-law providing for the purchase of this steamer was passed by the directors by a majority vote, Beatty's vote being necessary to make the majority. Under this by-law the contract of purchase was at once made. Later this by-law was submitted to the stockholders for ratification, and was ratified by a majority, Beatty's shares being a necessary part of the majority. The minority filed the bill, making the company and Beatty parties defendant. All question of fraud was eliminated from the case by the facts found by the inferior courts, and the decision both below and in the privy council was made to turn upon the single question as to whether Beatty could properly vote his stock in confirmation of the sale he had made. The court held that the original contract between the directors and Beatty could not have been enforced by Beatty in consequence of his fiduciary relations to the company as a director, but that any such dealing or arrangement might be affirmed or adopted by the company, provided it was not brought about by unfair means, and was not "illegal or fraudulent or oppressive towards those shareholders who opposed it." Finding that the contract was not oppressive or illegal or fraudulent, the court held that the case must turn upon the simple question as to whether Beatty, as a shareholder, might vote his shares in confirmation of what had been done. Upon this subject the court said:

"Unless some provision to the contrary is to be found in the charter or other instrument by which the company is incorporated, the resolution of a majority of the shareholders, duly convened, upon

any question with which the company is legally competent to deal, is binding upon the minority and consequently upon the company, and every shareholder has a perfect right to vote upon any such question, although he may have a personal interest in the subject-matter opposed to, or different from, the general or particular interests of the company."

Touching the possibility of an oppressive use of power by an interested majority of shareholders, the court said:

"The only unfairness or impropriety which, consistently with the admitted and established facts, could be suggested, arises out of the fact that the defendant J. H. Beatty possessed a voting power as a shareholder which enabled him, and those who thought with him, to adopt the by-law, and thereby either to ratify and adopt a voidable contract into which he, as a director, and his co-directors, had entered, or to make a similar contract; which latter seems to have been what was intended to be done by the resolution passed on the 7th of February. It may be quite right that in such a case the opposing minority should be able, in a suit like this, to challenge the transaction, and to show that it is an improper one, and to be freed from the objection that a suit with such an object can only be maintained by the company itself. But the constitution of the company enabled the defendant J. H. Beatty to acquire this voting power. There was no limit upon the number of shares which a shareholder might hold, and for every share so held he was entitled to a vote. The charter itself recognized the defendant as a holder of 200 shares, one-third of the aggregate number. He had a perfect right to acquire further shares, and to exercise his voting power in such a manner as to secure the election of directors whose views upon policy agreed with his own, and to support those views at any shareholders' meeting. The acquisition of the United Empire was a pure question of policy, as to which it might be expected that there would be differences of opinion, and upon which the voice of the majority ought to prevail. To reject the votes of the defendant upon the question of the adoption of the by-law would be to give effect to the views of the minority, and to disregard those of the majority."

A question of like character received very able consideration by the court of appeals of New York in *Gamble v. Water Co.*, 123 N. Y. 91, 25 N. E. 201, the opinion being by Justice Peckham. While upholding the general right of a majority stockholder to vote his stock in his own interest, the court said that the action resulting from such power "must not be so detrimental to the interests of the corporation itself as to lead to the necessary inference that the interests of the majority of the shareholders lie wholly outside of, and in opposition to, the interests of the corporation and of the minority of the shareholders, and that their action is a wanton or fraudulent destruction of the rights of such minority. In such cases it may be stated that the action of the majority of the shareholders may be

subjected to the scrutiny of a court of equity at the suit of the minority shareholders."

Touching the circumstances under which a dissenting minority might challenge a contract imposed upon the company by the vote of an interested majority shareholder, the learned court, after referring to *Transportation Co. v. Beatty*, 12 App. Cas. 589, said:

"I think that where the action of the majority is plainly a fraud upon, or, in other words, is really oppressive to, the minority shareholders, and the directors or trustees have acted with, and formed part of, the majority, an action may be sustained by one of the minority shareholders suing in his own behalf and in that of all others coming in, etc., to enjoin the action contemplated, and in which action the corporation should be made a party defendant. It is not, however, every question of mere administration or of policy in which there is a difference of opinion among the shareholders that enables the minority to claim that the action of the majority is oppressive, and which justifies the minority in coming to a court of equity to obtain relief. Generally, the rule must be that in such cases the will of the majority shall govern. The court would not be justified in interfering, even in doubtful cases, where the action of the majority might be susceptible of different constructions. To warrant the interposition of the court in favor of the minority shareholders in a corporation or joint-stock association, as against the contemplated action of the majority, where such action is within the corporate powers, a case must be made out which plainly shows that such action is so far opposed to the true interests of the corporation itself as to lead to the clear inference that no one thus acting could have been influenced by any honest desire to secure such interests, but that he must have acted with an intent to subserve some outside purpose, regardless of the consequences to the company and in a manner inconsistent with its interests. Otherwise the court might be called upon to balance probabilities of profitable results to arise from the carrying out of the one or the other of different plans proposed by or on behalf of different shareholders in a corporation, and to decree the adoption of that line of policy which seemed to it to promise the best results, or at least to enjoin the carrying out of the opposite policy. This is no business for any court to follow."

That the Louisville & Nashville Railroad Company had the power to acquire, hold, and vote shares in the capital stock of the Nashville, Chattanooga & St. Louis Railway Company cannot be successfully denied. Such a purchase was not in excess of its chartered power, for the express power was conferred by an amendment of its charter granted January 27, 1880. Comity requires that this charter power shall be recognized as valid if not opposed to some law or policy of the state creating the corporation in which stock has been acquired. It is impossible in the present state of Tennessee legislation to say that this charter power is either opposed to any law or policy of that state. Upon the contrary, section 17 of the special charter

granted to the Nashville, Chattanooga & St. Louis Railway Company expressly invites such ownership by providing that "any state or any citizen, corporation or company of this or any other state or country, may subscribe for and hold stock in said company, with all the rights and subject to all the liabilities of any other stockholder." In addition to this, Acts 1881, c. 9, authorizes all railroad companies, "existing under the laws of this state or of this state and any other state or states," to acquire, by "purchase or otherwise, and hold or dispose of, any bonds or shares of the capital stock of any railroad company or companies in any state or states." This provision does not cover the Louisville & Nashville Railroad Company, which is neither a corporation of this state nor of this and another state, but it indicates so broad a policy in respect to such transactions as to forbid the courts from saying that ownership of such shares is contrary to the public policy of this state. The right to own and vote this stock carries with it the right to vote for directors and to vote the stock upon all questions in which the owner has an interest. *Transportation Co. v. Beatty*, 12 App. Cas. 589; *Gamble v. Water Co.*, 123 N. Y. 91, 25 N. E. 201; *Beach Priv. Corp.* § 247; *Mor. Priv. Corp.* § 729.

That this majority of the stock has been used for the purpose of electing a board of directors selected by the majority owner is no cause for complaint. The majority, rather than the minority, are entitled to control, provided that control be not used oppressively, and for the outside and illegal purposes of obtaining unjust advantages at the expense of the legitimate interests of the minority.

* * * * *

That the directors of the Nashville, Chattanooga & St. Louis Railway Company were elected by this holder of a majority of the stock does not make them agents of that interest, nor raise any legal presumption that they are or will be unfaithful to the true and general interests of the corporation whose powers they exercise. *Trust Co. v. Bridges*, 16 U. S. App. 115-141, 6 C. C. A. 539, 57 Fed. 753. Inasmuch as a stockholder is not a trustee and holds and acts for himself alone, there is no rule which forbids his contracting with his own company. *Oil Co. v. Marbury*, 91 U. S. 587-589. But the majority shareholders will not be permitted to use this power of control for the purpose of obtaining advantages for themselves at the expense of the minority, and, when an unfair and oppressive contract is shown, a case is made which will authorize interference on behalf of the injured minority.

If it be true, as explicitly charged, that this majority of stock was purchased "for the purpose of overcoming a mischievous rival, and of increasing the revenues of the L. & N. R. R. Co., to the loss of the N., C. & St. L. Ry. Co.," and that this power of control has been used to impose upon the controlled company a disastrous contract, and thus accomplish the alleged purposes in acquiring control, it would, indeed, be unavailing to expect the controlling in-

fluences to institute such a suit as this, and rule 94 would have no application. *De Neufville v. Railroad Co.*, 26 C. C. A. 306, 81 Fed. 10, and 51 U. S. App. 374.

If it be true, as charged, that the lease now in question is so highly prejudicial to the true and exclusive interests of the lessee company as to greatly impair, if not destroy, its ability to continue to pay dividends then that fact will tend to establish the further charge that the true interests of the lessee company were not represented, and that the majority of the directors in consenting to so ruinous a contract intended to subserve the purposes and interests of the majority stockholder, regardless of consequences to the true and exclusive interests of the corporation whose power they were exercising. In the face of such averments as these, we cannot deny to the minority a right to challenge this contract in a suit of this character. If the averments and charges of the bill in this particular be true, the corporation is not able to prosecute or conduct this suit, being still under the control of the same influences which led to the original authorization of the contract. It would be a travesty upon justice to expect self-respecting managing officers to begin and prosecute a suit in which their own good faith and loyalty should be the principal question involved. Under these circumstances, this bill is rightly filed and no demand upon the officers of the corporation was necessary. The demurrer, going to the form and general equity of the bill, must be overruled.*

* *City of Chicago v. Cameron* (1887) 120 Ill. 447, 11 N. E. 899, *Accord. Cf. Squair v. Lookout Mtn. Co.* (1890) 42 Fed. 729.

Demand is unnecessary on proof that it would be vain and fruitless, *Weir v. Bay State Gas Co.* (1898) 91 Fed. 940, e. g., where collusion appears, *Brewer v. Boston Theatre* (1870) 104 Mass. 378, or conspiracy of fraudulent directors, *Harrison v. Thomas* (1901) 112 Fed. 22, 50 C. C. A. 98, or urgent emergency necessitates immediate action, *Starr v. Shepard* (1906) 145 Mich. 302, 108 N. W. 709. See also *Decatur Mineral Land Co. v. Palm* (1896) 113 Ala. 531, 21 So. 315, 59 Am. St. 140 (though appeal to stockholders useless, appeal to directors held necessary); *Green v. Hedenberg* (1896) 159 Ill. 489, 42 N. E. 851, 50 Am. St. 178; *Dunphy v. Travellers' Newspaper Assn.* (1888) 146 Mass. 495, 16 N. E. 426; *Shaw v. Staight* (1909) 107 Minn. 152, 119 N. W. 951, 20 L. R. A. (N. S.) 1077, and note, 9 Columbia Law Rev. 445; *O'Connor v. Virginia &c. Power Co.* (1904) 48 Misc. (N. Y.) 228, 92 N. Y. Supp. 161.

In *Bjorngaard v. Goodhue County Bank* (1892) 49 Minn. 483, 52 N. W. 48, Gilfillan, C. J. said: "The directors against whom complaint is made are not only a majority of the directors, but they own a majority of the stock, so that any application either to the board of directors or to the body of stockholders to bring the action would be equivalent to asking the alleged wrong-doers to bring suit in the name of the corporation against themselves. The law does not require of the minority stockholders to do so absurd a thing as a condition of seeking relief against the wrongful acts of the directors and majority stockholders."

In *Doherty v. Mercantile Trust Co.* (1904) 184 Mass. 590, 69 N. E. 335, held: "It is not enough to enable a stockholder to bring a bill to enforce in behalf of a corporation the rights which, if successful, will enure to the corporation, to make a naked request that such a bill should be brought without submitting to the directors the facts on which it could be maintained." (*per Loring, J.*, at p. 593).—Eds.

CONTINENTAL SECURITIES CO. v. BELMONT.

1912. 206 N. Y. 7, 99 N. E. 138.

ACTION by the Continental Securities Company and Clarence H. Venner, stockholders in the Interborough Rapid Transit Company, on behalf of themselves and of other stockholders similarly situated, and on behalf of the company, against August Belmont and others, impleaded with the Interborough Rapid Transit Company. From an order of the Appellate Division, affirming an order denying a motion by certain of the defendants for judgment upon the pleadings, defendants, other than the Interborough Rapid Transit Company, appeal by permission.

CHASE, J. This is a representative action derived from the Interborough Rapid Transit Company. It is brought in behalf of the plaintiffs and all others similarly interested, as stockholders of said company, against the directors of said company and said company to require said individual defendants to account to said company for fifteen thousand shares of its capital stock, alleged to have been issued fraudulently and illegally, and without any valid or adequate consideration therefor, but upon an alleged consideration that was a pretense and subterfuge and intended to cover a gift or bonus to the defendants Belmont and Luttgen, and their nominees, and also to require said individual defendants to account for the dividends which have been paid on said stock. It is alleged that by reason of the facts set forth in the complaint the defendant corporation has suffered damage to an amount exceeding \$4,500,000. Each of the defendants answered the complaint, and, after the answers were interposed, a motion was made for judgment upon the pleadings dismissing the complaint pursuant to section 547 of the Code of Civil Procedure, which motion was denied. An appeal was taken therefrom to the Appellate Division, where the order denying said motion was unanimously affirmed. Leave was granted by the Appellate Division to the defendants, other than the defendant company, to appeal to this court, and the following questions were certified:

"(1) Does the complaint state a cause of action?

"(2) Was the motion of the defendants for judgment against the plaintiffs on the pleadings rightfully denied?"

As the opinion will not discuss the complaint generally, but only in connection with the objections that are made to it by the appellants in this court, it is unnecessary to state its provisions except as required in considering such objections.

It appears from the complaint that each of the plaintiffs purchased his stock subsequently to the transactions complained of in the complaint. This court in the recent case of *Pollitz v. Gould*, 202 N. Y. 11, 94 N. E. 1088, has definitely determined that a stockholder may bring an action in behalf of the corporation for the benefit of himself and all other stockholders to set aside as fraudulent an im-

proper transaction consummated at the expense of the corporation before he acquired his stock.

It is alleged that the 15,000 shares of stock were issued pursuant to a resolution unanimously adopted by the directors of said company, of which the following is a copy, viz.: "Resolved that this company do purchase of August Belmont & Company one thousand nine hundred and seventy-five (1,975) shares of the capital stock of the Pelham Park Railroad Company of the par value of twenty-five dollars (\$25) per share; one thousand nine hundred and thirty-five (1,935) shares of the capital stock of the City Island Railroad Company of the par value of twenty-five dollars (\$25) per share; and twenty-seven thousand five hundred dollars (\$27,500) in the first mortgage bonds of the Pelham Park Railroad Company, for the sum of one million five hundred thousand dollars (\$1,500,000) to be paid by the issue and delivery of fifteen thousand (15,000) shares of the par value of one hundred dollars (\$100) each in the full-paid non-assessable capital stock of this company, to such persons and in such amounts as the said August Belmont & Company may direct; which said sum is also to cover full compensation to the said August Belmont & Company for their services in procuring the assignment of the contract between John B. McDonald and the city of New York aforesaid, the sale to this company of the stock of the Rapid Transit Subway Construction Company and the subscriptions to the remainder of the capital stock of this company." It is further alleged that the statement in said resolution in substance that said 15,000 shares of stock was to be issued and delivered in part to cover full compensation for certain alleged services rendered by the defendants Belmont and Luttgen was a pretense and subterfuge designed and intended to cover up the real transaction which was (except as to the actual cost of said stock and bonds of said railroad companies, namely, \$32,185.97) a gift or bonus to said defendants Belmont and Luttgen and their nominees of said stock in the defendant company.

The appellants assert that the complaint is fatally defective because it does not offer to return the stock and bonds described in said resolution. The action is not brought for a rescission of the contract with August Belmont & Co., but for an accounting. The plaintiffs are not in possession of said stocks and bonds, and as individual stockholders are unable through no fault of theirs to return them. The plaintiffs do not bring this action because their rights have been directly violated or because the cause of action is theirs, or because they are entitled to the relief sought. They are permitted to sue in this manner simply in order to set in motion the judicial machinery of the court. *Pomeroy's Equity Jurisprudence*, § 1095. The court in the action can preserve and adjust the equities of the parties to it. *Thompson on Corporations*, (2d Ed.) § 4568; 2 *Mechem on Corporations*, § 1179; *Kley v. Healy*, 127 N. Y. 555, 28 N. E. 593; s. c. 149 N. Y. 346, 44 N. E. 150; *Pritz v. Jones*,

117 App. Div. 643, 102 N. Y. Supp. 549; *Heckscher v. Edenborn*, 203 N. Y. 210, 96 N. E. 441. The actual value of said stocks and bonds can be found in the action, and, if equity requires it, the defendant corporation can be directed to return such stocks and bonds to said August Belmont & Co.

It was not necessary for the plaintiffs to allege in the complaint that their predecessors in title did not assent to or acquiesce in the alleged fraudulent issue of said 15,000 shares of stock. It is not necessary to negative such assent or acquiescence in a fraud, unless it is otherwise to be presumed from the delay in bringing the action or generally from the allegations of the complaint. If it exists, it is a matter of defense. *Sage v. Culver*, 147 N. Y. 241, 41 N. E. 513; *Pollitz v. Gould*, *supra*. If the rule were otherwise, the objection to the complaint would not avail the defendants in this case because the allegations of the complaint amount to a negative of any assent by the plaintiffs or their predecessors in title to the transactions alleged in the complaint.

It is also claimed by the appellants that it does not appear from the complaint that the defendant corporation and its board of directors were requested to bring suit to recover said fifteen thousand shares of stock or the value thereof, or that said corporation or said board of directors neglected or refused to bring such action. It appears from the complaint that on the 12th day of March, 1910, the plaintiff corporation, then being the owner of the stock now owned by the two plaintiffs, delivered to the defendant corporation and to its officers and directors a written communication directed to said defendant corporation and its president and directors, calling attention to the fact of the issue and delivery of said 15,000 shares of capital stock for a grossly inadequate and illegal consideration, and requesting and demanding that suit be brought in behalf of the corporation and in good faith prosecuted against the incorporators of said company and members of its board of directors during the year 1902 and said firm of August Belmont & Co. to recover the damages suffered by reason of the action of the said incorporators and directors.

Said written communication also stated and provided as follows: "We hereby offer to properly indemnify the Interborough Rapid Transit Company against any damage or costs it may sustain as a result of bringing and prosecuting such suit. A copy of this letter is mailed to each director of the Interborough Rapid Transit Company. Unless within ten days from date you advise us that the request and demand herein will be complied with we shall conclude that you refuse." Thereafter the plaintiffs waited until May 4, 1910, when, no action having been commenced and no response having been made to said written communication, this action was commenced.

Upon the facts so alleged the plaintiffs treated the defendant corporation and its board of directors as having refused and neg-

lected to bring such action and the allegations relating thereto are sufficient to sustain the complaint. *Kavanaugh v. Commonwealth Trust Co.*, 103 App. Div. 95, 92 N. Y. Supp. 543.

On this appeal as on the motion at the Special Term and on the hearing of the appeal in the Appellate Division the allegations of the complaint are taken as true.

It is conceded that an action in equity cannot be maintained by the plaintiffs as individual stockholders for themselves and all others similarly interested, unless it is necessary because of the neglect and refusal of the corporate body to act.

It is necessary, therefore, in an action by the plaintiffs to set forth two things: First, a cause of action in favor of the corporation with the same detail of facts as would be proper in case the corporation itself had brought the action; second, the facts which entitle the plaintiff to maintain the action in place of the corporation.

Kavanaugh v. Commonwealth Trust Co., 181 N. Y. 121, 73 N. E. 562; *O'Connor v. Virginia Passenger & Power Co.*, 184 N. Y. 46, 76 N. E. 1082. It is not seriously contended that the complaint does not state a good cause of action in favor of the defendant corporation. It is insisted by the defendants that it was necessary for the plaintiffs, in addition to alleging a demand upon the defendant corporation and its board of directors to bring the action and their neglect and refusal to do so, to allege that they had given notice of the alleged fraud to the body of stockholders of the defendant corporation, and had demanded of said stockholders that some action be taken by them to redress the wrong, and that such body of stockholders had neglected and refused to take any action relating thereto. The cause of action belongs to the corporate body and not to the plaintiffs and other stockholders individually, nor to the body of stockholders collectively.

The board of directors represents the corporate body. It is provided by statute in this state that the affairs of every corporation shall be managed by its board of directors. General Corporation Law (Consol. Laws 1909, c. 23) § 34. The directors are not ordinary agents in the immediate control of the stockholders. The directors hold their office charged with the duty to act for the corporation according to their best judgment, and in so doing they cannot be controlled in the reasonable exercise and performance of such duty. The corporation is the owner of the property, but the directors in the performance of their duty possess it and act in every way as if they owned it. *People ex rel. Manice v. Powell*, 201 N. Y. 194, 94 N. E. 634. They are trustees clothed with the power of controlling the property and managing the affairs of a corporation without let or hindrance. As to third persons they are its agents, but as to the corporation itself equity holds them liable as trustees. 2 *Pomeroy's Equity Jurisprudence*, §§ 1061, 1073, 1088, 1097; *People ex rel. Manice v. Powell*, supra.

The claim of the appellants that the body of stockholders has

some immediate or direct authority to act for the corporation or to control the board of directors in the matters set forth in the complaint is based upon an erroneous conception of the duties and powers of the body of stockholders in this state.

As a general rule, stockholders cannot act in relation to the ordinary business of a corporation. The body of stockholders have certain authority conferred by statute which must be exercised to enable the corporation to act in specific cases, but except for certain authority conferred by statute, which is mainly permissive or confirmatory, such as consenting to the mortgage, lease, or sale of real property of the corporation, they have no express power given by statute. They are not by any statute in this state given general power of initiative in corporate affairs. Any action by them relating to the details of the corporate business is necessarily in the form of an assent, request, or recommendation. Recommendations by a body of stockholders can only be enforced through the board of directors, and indirectly by the authority of the stockholders to change the personnel of the directors at a meeting for the election of directors. Such action may or may not result in securing adequate, corporate action with reference to illegal or fraudulent acts. For reasons wholly apart from the matter in dispute, the stockholders may not desire to change a majority of the persons comprising its board of directors. Some of the reasons why the power vested in stockholders to elect directors is inadequate as a remedy for specific fraudulent acts are stated by Cook in his work on *Stock and Stockholders*, § 740, in which he says: "There has been considerable discussion as to whether the stockholder in addition to his request to the corporate officers to institute the suit should not also be required to attempt to induce the stockholders in meeting assembled to take action by directing the directors to bring suit, or by refusing to re-elect them at the next election. The facts, however, that the stockholders in meeting assembled cannot control the discretion of the directors in bringing such a suit, that the remedy of refusing to re-elect them involves delay, and the assumption that a minority of the stockholders can by the election control such a suit, that irreparable injury or the vesting of great financial interests may occur in the meantime, and that laches may arise as a bar to the stockholder's suit, have settled the rule that the stockholder's request to the corporate directors to institute the suit is sufficient. He need not also apply to a stockholders' meeting." Although it is said that the authority of stockholders in the management of business corporations is exhausted when they elect the directors (*Thompson on Corporations* [2d Ed.], § 1178), nevertheless it is generally recognized that certain acts of boards of directors that are legal, but voidable, can be ratified and confirmed by a majority of the body of stockholders as the ultimate parties in interest and thus make them binding upon the corporation. *Morawetz on Corporations* (2d Ed.), §§ 625, 626. Such recognized authority in stockholders

to ratify and confirm the acts of boards of directors is confined to acts voidable by reason of irregularities in the make-up of the board or otherwise or by reason of the directors or some of them being personally interested in the subject-matter of the contract or act, or for some other similar reason which makes the action of the directors voidable. No such authority exists in case of an act of the board of directors which is prohibited by law or which is against public policy. *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159.

In any case where action is taken by stockholders confirming and ratifying a fraud and misapplication of the funds of the corporation by the directors or others the action is binding only by way of estoppel upon such stockholders as vote in favor of such approval. *Morawetz on Corporations* (2d Ed.), § 625. The distinction between acts that can and those that cannot be confirmed and ratified is shown in the report of two frequently cited English decisions, namely, *Foss v. Harbottle*, 2 Hare, 461, and *Bagshaw v. Eastern Union Railway Co.*, 7 Hare, 114. The former of these cases was limited to the approval of a legal but voidable act. In the *Bagshaw Case*, where the directors of a corporation had misapplied or were about to misapply certain moneys of the corporation, the court say: "No majority of the shareholders, however large, could sanction the misapplication of this portion of the capital. A single dissenting voice would frustrate the wishes of the majority. Indeed, in strictness, even unanimity would not make the act lawful. This appears to me to take it out of the case of *Foss v. Harbottle*, to which I was referred. That case does not, I apprehend, upon this point, go further than this: That if the act, though it be the act of the directors only, be one which a general meeting of the company could sanction, a bill by some of the shareholders on behalf of themselves and others, to impeach that act, cannot be sustained, because a general meeting of the company might immediately confirm and give validity to the act of which the bill complains."

It is the governing body or bodies of a corporation with power to enforce a remedy to whom complaining stockholders must go with their demand for relief. The governing body of corporations in this state, as we have seen, is the board of directors. A complaining stockholder must go to such board for relief before he can bring an action, unless it clearly appears by the complaint that such application is useless. If the subject-matter of the stockholder's complaint is for any reason within the immediate control, direction, or power of confirmation of the body of stockholders, it should be brought to the attention of such stockholders for action, before an action is commenced by a stockholder unless it clearly appears by the complaint that such application is useless. The decision reported in *Hawes v. Oakland*, 104 U. S. 450, 26 L. Ed. 827, and other similar decisions in the federal and state courts are not in conflict with the decision about to be rendered herein. In such cases, as in this case, it is asserted that an application to the body of stockholders

is unnecessary when it is unreasonable to require it. If the body of stockholders has no adequate power or authority to remedy the wrong asserted by the individual stockholders, it is unreasonable and unnecessary to require an application to it to redress the wrong before bringing a representative action. See opinion of Carr, J., in the Appellate Division herein (Sup.) 134 N. Y. Supp. 635. See, also, *Delaware & H. Co. v. Albany & S. R. R. Co.*, 213 U. S. 435, 29 Sup. Ct. 540, 53 L. Ed. 862. In this case, where the plaintiff alleges fraud and a substantial misappropriation of 15,000 shares of the stock of the corporation through a nominal purchase of property and the payment of a pretended claim for services, application to the body of stockholders was not necessary.

It is claimed by the respondents that the complaint discloses such a state of facts as would dispense with the necessity of making any demand either upon the corporation, its board of directors, or the body of stockholders before bringing an action to recover for the company the value of the 15,000 shares of stock alleged to have been illegally and fraudulently issued to the individual defendants.

We have not considered the allegations of the complaint with reference to such claim of the respondents.

The order should be affirmed, with costs, and each of the questions certified answered in the affirmative.

CULLEN, C. J., and GRAY, HAIGHT, VANN, WERNER, and WIL-LARD BARTLETT, JJ., concur.

*Order affirmed.*¹

¹ *Cf. Sage v. Culver* (1895) 147 N. Y. 241, 41 N. E. 513.

"As a general rule courts have nothing to do with the internal management of business corporations. Whatever may lawfully be done by the directors or stockholders, acting through majorities prescribed by law, must of necessity be submitted to by the minority, for corporations can be conducted upon no other basis. All questions within the scope of the corporate powers which relate to the policy of administration, to the expediency of proposed measures, or to the consideration of contracts, provided it is not so grossly inadequate as to be evidence of fraud, are beyond the province of the courts. The minority directors or stockholders cannot come into court upon allegations of a want of judgment or lack of efficiency on the part of the majority and change the course of administration. Corporate elections furnish the only remedy for internal dissensions, as the majority must rule so long as it keeps within the powers conferred by the charter.

"To these general rules, however, there are some exceptions, and the most important is that founded on fraud. While courts cannot compel directors or stockholders, proceeding by the vote of a majority, to act wisely, they can compel them to act honestly, or undo their work if they act otherwise. Where a majority of the directors, or stockholders, or both, acting in bad faith, carry into effect a scheme which, even if lawful upon its face, is intended to circumvent the minority stockholders and defraud them out of their legal rights, the courts interfere and remedy the wrong. Action on the part of directors or stockholders, pursuant to a fraudulent scheme designed to injure the other stockholders, will sustain an action by the corporation, or, if it refuses to act, by a stockholder in its stead for the benefit of all the injured stockholders." *Per Vann, J.*, in *Flynn v. Brooklyn City R. Co.* (1899) 158 N. Y. 493, at pp. 507-8, 53 N. E. 520.

See also *Niles v. N. Y. Central & C. R. Co.* (1903) 176 N. Y. 119, 68 N. E. 142; *Jacobson v. Brooklyn Lumber Co.* (1906) 184 N. Y. 152, 76 N. E. 1075;

HOME FIRE INS. CO v. BARBER.

1903. 67 Neb. 644, 93 N. W. 1024.^s

THIS was a suit by a corporation to recover from the defendant, one of the original incorporators and a stockholder, director and general manager of the company, for mismanagement, and for profits made by him through the use of the company's money.

POUND, C.—Sound reason and good authority sustain the rule that a purchaser of stock cannot complain of the prior acts and management of the corporation. *Hawes v. Contra Costa Water-works Co.*, 104 U. S. 450, 26 L. ed. 827; *Dimpfell v. Ohio & M. R. Co.*, 110 U. S. 209, 3 Sup. Ct. Rep. 573, 28 L. ed. 121; *Taylor v. Holmes*, 127 U. S. 489, 8 Sup. Ct. Rep. 1192, 32 L. ed. 179; *Southwest Natural Gas Co. v. Fayette Fuel-Gas Co.*, 145 Pa. St. 13, 23 Atl. Rep. 224; *Alexander v. Searcy*, 81 Ga. 536, 8 S. E. Rep. 630, 12 Am. St. Rep. 137; *Clark v. American Coal Co.*, 86 Ia. 436, 53 N. W. Rep. 291, 17 L. R. A. 557; *United Electric Securities Co. v. Louisiana Electric Light Co.*, 68 Fed. Rep. 673; *Venner v. Atchison, T. & S. F. R. Co.*, 28 Fed. Rep. 581; *Heath v. Erie R. Co.*, 8 Blatchf. (U. S. C.) 347, Fed. Cas. No. 6,306; *Dannmeyer v. Coleman*, 8 Sawy. (U. S. C. C.) 51, 11 Fed. Rep. 97; *Pennsylvania Tack Works v. Sowers*, 2 Walk. (Pa.) 416; 4 *Thompson Corporations*, sec. 4569. In *Alexander v. Searcy*, supra, the court say (p. 550): "The weight of authority seems to be that a person who did not own stock at the time of the transactions complained of, cannot complain or bring a suit to have them declared illegal." In *United States Securities Co. v. Louisiana Electric Light Co.* it is said (p. 675): "As a general proposition, the purchaser of stock in a corporation is not allowed to attack the acts and management of the company prior to the acquisition of his stock; otherwise, we might have a case where stock duly represented in a corporation consented to and par-

Continental Ins. Co. v. N. Y. & C. R. Co. (1907) 187 N. Y. 225, 79 N. E. 1026; *Pollitz v. Wabash R. Co.* (1912) 150 App. Div. (N. Y.) 715, 135 N. Y. S. 785, modified (1912) 100 N. E. 721.

NOTE ON STOCKHOLDERS' DERIVATIVE SUITS.

In a stockholder's suit, the corporation is a necessary party defendant. *Davenport v. Dows*, (1873) 18 Wall. (U. S.) 626, 21 L. ed. 938.

The misconducting directors must also be parties. *Edwards v. Bay State Gas Co.*, (1898) 91 Fed. 942.

The corporation, although the real plaintiff, is not regarded as such for the purposes of jurisdiction of the United States courts. *Doctor v. Harrington*, (1904) 196 U. S. 579, at pp. 587-589, 25 Sup. Ct. 355, 49 L. ed. 606.

The plaintiff must make out a cause of action in favor of the corporation, where suing in a representative capacity. *Waters v. Waters & Co.*, (1911) 201 N. Y. 184, 94 N. E. 602.

The plaintiff must sue on behalf of himself and all other stockholders, as representative of their aggregate rights. *McAfee v. Zettler* (1897) 103 Ga. 579, 30 S. E. 268.—Eds.

^sStatement of facts abridged from that in the opinion. Only portions of the opinion are given.—Eds.

ticipated in bad management and waste and, after reaping the benefits from such transactions, could be easily passed into the hands of a subsequent purchaser, who could make his harvest by appearing and contesting the very acts and conduct which his vendor had consented to." These remarks are not without application to the case at bar. The present shareholders are all subsequent purchasers; they obtained their stock through the defendant Barber; they hold a large number of their shares under a purchase from him and his associates through the very mismanagement now complained of; a majority of the remaining shares come directly from Barber and his associates in the wrongs upon which his suit is based. In other words, the present stockholders are contesting acts through which they get title to a large portion of their stock, and acts which those through whom they derived the greater part of the remainder could not have challenged because they participated therein, and, by contesting these acts, which did not injure any of the present stockholders in the least, are recovering back a large part of the purchase price of stock which was admittedly worth all that they paid for it. Such cases illustrate forcibly the wisdom of confining complaint of this kind to those who were stockholders at the time or their successors by operation of law.

The rule that a suit for mismanagement cannot be maintained by one who was not a stockholder at the time, has been criticised as based on jurisdictional considerations peculiar to the Federal courts and on obsolete common-law doctrines as to champerty and maintenance. 4 Thompson, Corporations, secs. 4569-4571; 1 Morawetz, Private Corporations, sec. 270. In our judgment it does not depend upon either.

* * * * *

The right of the stockholder to sue exists because of special injury to him for which otherwise he is without redress. If his interest is trifling and the injury thereto of no consequence, he cannot sue to compel righting of wrongs to the corporation. McHenry v. New York, P. & O. R. Co., 22 Fed. Rep. 130; Albers v. Merchants' Exchange of St. Louis, 45 Mo. App. 206. Hence there is obvious reason for holding that one who held no stock at the time of the mismanagement ought not to be allowed to sue unless the mismanagement or its effect continue and are injurious to him, or it affects him specially and peculiarly in some other manner. City of Chicago v. Cameron, 22 Ill. App. 91, 120 Ill. 447, 11 N. E. Rep. 899, is a case of the first type; Carson v. Iowa City Gaslight Co., 80 Ia. 638, 45 N. W. Rep. 1068, is one of the second type. Except in such cases, the purchaser ought to take things as he found them when he voluntarily acquired an interest. If he was defrauded in the purchase, he should sue the vendor. As to the corporation and its managers, so long as he is not injured in what he got when he purchased, and holds exactly what he got and in the condition in which he got it,

there is no ground of complaint. *Clark v. American Coal Co.*, 86 Ia. 436, 53 N. W. Rep. 291, 17 L. R. A. 557.

But it may be doubtful whether a purchaser of stock buys or intends to buy anything beyond the vendor's present interest in the corporation and its assets. His vendor's causes of action for past injuries and rights to complain of past mismanagement are scarcely in contemplation of the parties. We must not suffer ourselves to be deceived by speaking of causes of action of the corporation in this connection, since causes of action of this character belong to the corporation for the benefit and in the interest of its stockholders.

* * * * *

The fallacy in the view that one who has not been injured by a transaction and is not affected thereby can acquire a right to sue in equity to set it aside because he has acquired the shares of the person injured, is exposed in such cases as *Graham v. LaCrosse & M. R. Co.*, 102 U. S. 148, 26 L. ed. 106, and *Hoffman v. Bullock*, 34 Fed. Rep. 248. The right to complain of such transactions is one which the stockholders injured may or may not exercise as they choose. Where such transactions are not absolutely void, they may, if they so elect, acquiesce and treat them as binding. The discretion whether to sue to set them aside or to acquiesce in and agree to them is incapable of transfer. If the new stockholder is injured, there is another question. In that case he also has a power of proceeding or remaining inactive as he may prefer. Where he is not injured, he can take no advantage of the power which was in his vendor and the latter did not care to exercise.

* * * * *

It appears to be well settled, also, that stockholders who have acquired their shares and their interest in the corporation from the alleged wrong-doers and through the prior mismanagement have no standing to complain thereof. *Brown v. Duluth, M. & N. R. Co.*, 53 Fed. Rep. 889; *Matter of Application of Syracuse, C. & N. Y. R. Co.*, 91 N. Y. 1; *Schilling & Schneider Brewing Co. v. Schneider*, 110 Mo. 83, 19 S. W. Rep. 67; *Langdon v. Fogg*, 14 Abb. N. Cas. (N. Y.) 435; *Parsons v. Hayes*, 18 Jones & Sp. (N. Y.) 29; *Hollins v. St. Paul, M. & M. R. Co.*, 9 N. Y. Supp. 909; *Clark v. American Coal Co.*, 86 Ia. 436, 53 N. W. Rep. 291, 17 L. R. A. 557; 4 *Thompson, Corporations*, p. 3410; *Cook, Corporations*, secs. 40, 736, note. If a stockholder's predecessor in title has acquiesced in a course of mismanagement, it has even been held that he cannot maintain a suit to restrain its continuance. *Trimble v. American Sugar Refining Co.*, 61 N. J. Eq. 340, 48 Atl. Rep. 912. In *Thompson, Corporations, supra*, the learned author says (p. 3409): "But as share certificates do not, under any theory, rise to the grade of strictly negotiable paper, it should follow, and especially in regard to the transfer of any litigious rights which may attach to them, that their holder cannot, by selling them to another, transfer to that other any better

Dec.
this case
based
this rule

litigious rights, inhering in them, than he himself possesses. [If, therefore, he has, by his conduct as a shareholder, estopped himself from maintaining a suit in equity to undo corporate action, * * * this estoppel will attend the shares in the hands of his vendee."] In consequence, it would make no great difference in the case at bar, as to the standing of the present shareholders of the company in a court of equity, if we held that subsequent shareholders could attack prior mismanagement. The present shareholders hold 260 shares through a purchase from Barber, who acquired title through the acts complained of, and the money which they paid for those very shares, which they hold through such purchase, is now claimed to belong to the corporation, and is sought to be recovered from their vendor. Nor is this all. The greater part of the remaining shares were held by Barber and his associates when the alleged wrongs were committed, and are now held by the present stockholders under a purchase from Barber. To allow them to open up these transactions is to allow them to go counter to their own title to a large part of the stock, and to assert rights and claims which their vendor could never have asserted, and this, too, as to past transactions, which have no present effect upon the value of their stock, and do not continue to be felt in any way in the corporate management. * * *

POLLITZ v. GOULD.

1911. 202 N. Y. 11, 94 N. E. 1088.

APPEAL, by permission, from an order of the Appellate Division of the Supreme Court in the first judicial department, entered January 13, 1911, which affirmed an order of Special Term denying a motion to dismiss the complaint upon the pleading.

The following questions were certified: "1. Does the fact that the plaintiff acquired his stock of the defendant, the Wabash Rail-

* That a transferee of stock, after the action complained of, cannot sue, see, *accord*, *Boldenweck v. Bullis* (1907) 40 Colo. 253, 90 Pac. 634. But see *Forrester v. Boston & C. Mining Co.* (1898) 21 Mont. 544, 55 Pac. 229, differentiating Federal cases decided under Equity Rule No. 94, now No. 27; and article in 21 Harv. Law Rev. 195.

(That disqualification of transferrer to sue is a good defense see) *Ffooks v. South Western R. Co.* (1853) 1 Sm. & Giff. 142, 17 Jur. 365; *Babcock v. Farwell* (1910) 245 Ill. 14, 91 N. E. 683; *Trimble v. American Sugar Refining Co.* (1901) 61 N. J. Eq. 340, 48 Atl. 912 ("bound by the acquiescence of his predecessor in title"); *McCampbell v. Fountain Head R. Co.* (1903) 111 Tenn. 55, 77 S. W. 1070, 102 Am. St. 731. But see, *contra*, *Parsons v. Joseph* (1891) 92 Ala. 403, 8 So. 788, holding that a *bona fide* assignee of an acquiescing stockholder can sue. *Cf.* *Clark v. American Coal Co.* (1892) 86 Iowa 436, 446-7, 53 N. W. 291, 17 L. R. A. 557.

In *Babcock v. Farwell*, *supra*, the court says at p. 41: "Neither can an assignee of stock maintain a suit in regard to transactions with the corpora-

road Company, upon which he bases his right to ask the court to enforce a cause of action in favor of the railroad company against the individual defendants, after all the transactions which the plaintiff insists imposed a liability in favor of the railroad company against the individual defendants had been consummated, all stocks and bonds issued and the transactions complained of in all respects completed, prevent the plaintiff from maintaining this action?

"2. Is the enforcement of such a cause of action confined to stockholders who actually owned stock at the time the transactions complained of were consummated and completed?"

The nature of the action and the facts, so far as material, are stated in the opinion.

Hiscock, J.—This action was brought by plaintiff as a stockholder in the Wabash Railroad Company in behalf of said company for the benefit of himself and all other stockholders to set aside as fraudulent a transfer and exchange of several millions of dollars par value of its stock for an equivalent amount of the capital stock of the Wabash Pittsburg Terminal Railway Company. It is necessary to go into the details of the transaction which is being attacked by the plaintiff through and in behalf of the company, for the sole question presented for our consideration may be discussed without doing this. This question is whether a stockholder may bring an action of this character for the purpose of avoiding an improper transaction consummated at the expense of the corporation before he acquired his stock, and as presented here the question is unembarrassed by any incidental considerations, as, that the prior holder of the stock consented to the transaction or that plaintiff's subsequent acquisition of the stock was accompanied by any circumstances which would render it inequitable for him to seek relief.

While somewhat strangely this question does not appear to have been decided by this court, it has been passed on by the lower courts of this state and by those of many other states and by the Supreme Court of the United States. It has also been somewhat considered by the courts of England. Conflicting conclusions have been reached by these decisions. Without reviewing the English authorities, which so far as cited do not seem to be very decisive, reference may be made to the decisions in this country.

The question was presented in *Hawes v. Oakland* (104 U. S. 450), and it was there held that a stockholder might not bring an action in behalf of the corporation to avoid a fraudulent transaction consummated before he acquired his stock. While the question was directly passed on it is fair to state that it was not considered at any great length and that the court seems to have been more concerned with

tion done or assented to by his assignor. The purchaser of shares of stock acquires no greater rights than his vendor. He holds by the same title and subject to the same liability. Shares of stock are merely choses in action, and the successive owners acquire only the rights held by their predecessors in title."—Eds.

establishing this rule as one of practice than of substantive law. The decision resulted in the adoption of a rule requiring the plaintiff in such an action to show before bringing suit that he owned the stock on which it was brought at the time the transaction complained of occurred, and whether it be regarded as establishing a principle of law or a rule of practice this authority has been subsequently followed in the United States courts.

In addition, this rule in such a stockholder's action has been approved in the following cases: *Alexander v. Searcy* (81 Ga. 536); *Boldenweek v. Bullis* (40 Colo. 252); *Rankin v. S. W. B. & I. Co.* (12 N. Mex. 54); *Moore v. Silver Valley Co.* (104 N. C. 534); *Clark v. American Coal Co.* (86 Ia. 436); *Home Fire Ins. Co. v. Barber* (67 Nebr. 644).

The contrary doctrine that a stockholder acquiring his stock subsequent to the occurrence complained of may maintain this character of an action has been affirmed in the following cases outside of this state: *Winsor v. Bailey* (55 N. H. 218); *City of Chicago v. Cameron* (22 Ill. App. 91; affirmed, 120 Ill. 447); *Montgomery Light & Power Co. v. Lahey* (121 Ala. 131); *Forrester v. B. & I. M., etc., Co.* (21 Mont. 544, 565); *Just v. Idaho, etc., Co.* (102 Pac. Rep. 381); *Rafferty v. Donnelly* (197 Pa. 423); *Appleton v. Am. Malting Co.* (65 N. J. Eq. 375).

It has also been approved in this state directly or indirectly in the following cases: *Ramsey v. Gould* (57 Barb. 398); *Young v. Drake* (8 Hun 61); *Ervin v. Oregon Ry. & N. Co.* (35 Hun 544); *Frothingham v. Broadway & Seventh Ave. R. R. Co.* (9 Civ. Pro. Rep. 304); *Sayles v. Central Nat. Bank* (18 Misc. Rep. 155); *O'Connor v. Virginia P. & P. Co.* (46 Misc. Rep. 530, 535).

Assuming this question to be an open one in this court, we have no hesitation in approving the rule which has heretofore prevailed in this state, that in the absence of special circumstances this character of action may be maintained by a stockholder acquiring his stock subsequent to the transaction which is challenged rather than the contrary one prevailing elsewhere. We do this not only because a long and uniform line of decisions by our own courts ought to have weight, but because the rule established by these decisions seems to be the sounder one.

A stockholder has an indivisible interest in the property and assets of a corporation subject to the discharge of its obligations. This indivisible interest generally speaking is represented by certificates of stock and is transferred by their transfer. The general character of these certificates and the effect of their transfer in passing the interest of the holder is too well established and understood to require any discussion. As an original proposition it would seem to be clear that a right of action by or in behalf of the corporation for fraud to set aside a conveyance of its assets or to avoid obligations imposed upon it is part of its rights, property and assets in which a stockholder has this indivisible interest transferable by the

transfer of his certificates. I am unable to see any real or substantial distinction by virtue of which a stockholder transferring his certificates would transfer all of his indivisible interest in bonds or real estate on hand, but would not transfer his interest in a right of action to recover bonds or real estate which had been fraudulently withdrawn from the possession of the corporation, and which it was entitled to recover. And if the subsequent holder by acquiring the certificates does acquire such latter interest, it seems to follow that he may if necessary, in behalf of the corporation, assert and prosecute an action to protect and enforce the same.

Brief reference may be made to some of the reasons advanced in opposition to this view. Counsel points out practical inconvenience which he says will result from its application owing to the difficulties in tracing stock and distinguishing that which has not assented to the transaction from that which has or from that which perhaps has been issued since its consummation. These arguments, however, are so counterbalanced by corresponding claims from the opposite standpoint as to be of little weight.

Again, it is argued that if one buys stock subsequent to the transaction he should be regarded as buying subject to it and not be permitted to question it. If the prior holder should give binding consent to the transaction, this under certain circumstances undoubtedly would prevent the subsequent purchaser from questioning it. But, in the absence of special circumstances, I fail to see any principle of estoppel or logic which makes a subsequent purchase of stock so subject to a fraudulent corporate transaction that the purchaser may not insist upon its being set aside. There is scarcely any analogy between the situation of one who buys from an individual some property which has been subjected to a transaction which has not been disaffirmed and that of one who purchases stock in a corporation which has the continuing right both before and after the purchase to disaffirm a wrong which has been perpetrated on it by its agents. There is little or no basis for the practical consideration that one who buys stock should be deemed to have adjusted his price to an existing transaction even though voidable. If he knows of it he may just as properly be assumed to have adjusted his price to the knowledge that the transaction may still be disaffirmed and avoided.

Then, lastly, an argument is made which seems to be founded on the idea that in order to bring an action of this nature the stockholder must in effect disaffirm the corporate transaction and that this disaffirmance involves a personal right of election which vests in the one holding the stock when the transaction is consummated and which cannot be transferred. It is said "the right to question a fraud is not a purchasable commodity," and is not "capable of assignment and transfer," and does not pass "as an implied incident to every sale of corporate stock," and this view seems to be supported by some of the many cases which have been collected and reviewed by counsel with manifest industry and care.

So far as this argument means to assert that a mere naked right to question a corporate transaction could not be transferred to a stranger, if such an attempt can be conceived of, it may be assumed to be true. But the assertion that the right to protect stock by procuring an improper corporate transaction to be vacated does not pass on a transfer of the stock is a very different proposition.

The election to disaffirm a fraudulent corporate transaction belongs to and is exercised in the right and name of the corporation and not of the stockholder. The stockholder demands that the right shall be exercised and the cause of action be prosecuted by the corporation or does it himself for the corporation. It is conceded that the one holding the stock when the fraud is consummated has this right. When he transfers his certificates the transaction still stands a continuing wrong impairing the surplus of the company and affecting the stock. If the transferee has the right to have it avoided this will protect and increase the value of his stock. If he has not acquired this right it is the only one held by his predecessor in or through the corporation, which has been thought of, which has not been transferred by the transfer of the stock. It will be an anomalous exception if the prior holder retains the right to maintain or have maintained this action while he passes all of his other rights by the transfer of his stock. The only justification pleaded for this is the idea suggested of a personal and non-transferable right of election to disaffirm vested in the original holder. But this theory is entirely unsubstantial. [Such prior holder does not acquire this right to object to the transaction and bring an action to set it aside as a power conferred upon him by reason of any personal qualities, but because of his character as a stockholder, and when he loses this character and transfers it to another with his stock there is no reason why the latter should not exercise the right as a proper and necessary incident to his stock ownership.]

The order should be affirmed, with costs, and both questions certified to us answered in the negative.

CULLEN, Ch. J., VANN, WERNER, WILLARD BARTLETT and CHASE, JJ., concur; HAIGHT, J., absent.

Order affirmed.

RABE v. DUNLAP.

1893. 51 N. J. Eq. 40, 25 Atl. 959.¹⁰

VAN FLEET, V. C.

THIS is an application for an injunction. The application is resisted on the ground that the complainants have, by their laches, lost all right to either temporary or permanent relief, the contention being that they are not entitled to an injunction now, nor can any re-

¹⁰ The statement of facts in the opinion is condensed from that in the original.—Eds.

lief be given them on final hearing. The only question, however, before the court at this time is, whether or not an injunction should issue. The facts to be considered in deciding this question are almost entirely free from dispute.

The facts briefly stated are: The complainants in this case are stockholders in the Lake Hopatcong Land and Improvement Company, incorporated in 1855, for the purpose of buying and selling land and erecting buildings on and about Lake Hopatcong. Some of the persons interested in this corporation organized three others, one to buy land and erect hotels and cottages and carry on the business of innkeeper, one to carry on the business of transporting passengers and merchandise, and one for the purpose of buying land, erecting hotels and leasing them. Under and pursuant to the provisions of a statute passed in 1888, these four corporations, in 1888, consolidated with the consent of a majority of the stockholders, given at a meeting duly called for that purpose, under the name of the Breslin Hotel and Land Company; and the property of the four corporations was thereupon conveyed to the new corporation, the Breslin Hotel and Land Company. The complainants knew of the meeting but did not attend.

The complainants, by bill brought in 1892, pray, among other things, that the new corporation may be declared to have been void from the beginning; that the deed by which the property of the corporation in which they are interested was conveyed to the new corporation may be declared to be a nullity, and that the property conveyed by it may be restored to the grantor or to a trustee to be appointed for that purpose; that the new corporation may be required to account for all property of their corporation which it has disposed of; that certain mortgages given to the defendant Dunlap may be decreed to be no lien on the land which their corporation conveyed to the new corporation; that said Dunlap may, in addition, be commanded and required to execute a release, releasing such land from the operation of his mortgages; and that, in the meantime and as preliminary to the principal relief sought, the further prosecution of his foreclosure suit in this court may be stayed or restrained.

(The learned Vice-Chancellor, after holding that the acts complained of were *ultra vires* and not binding on non-assenting stockholders, proceeded:)

But stockholders, to be entitled to the summary interference of the court in cases where they seek protection against acts which are merely in excess of the power of the corporation, and are not prohibited by law, must be diligent; they must apply so recently after the doing of the act of which they complain that the court may stop or undo the wrong to them without doing equal or greater wrong to some other person. The principle which must control the action of a court of equity, in cases where the defense is laches, was laid down by Lord Camden, many years ago, in these words: "Nothing can

call forth the activity of a court of equity but conscience, good faith, and reasonable diligence. Where these are wanting the court is passive, and does nothing. Laches and neglect are always discountenanced, and therefore from the beginning of this jurisdiction there was always a limitation to suits in equity." *Smith v. Clay*, reported in a note to *Deloraine v. Browne*, 3 Bro. C. C. 639 (Amb. 645). This principle, as it is applied to stockholders who are tardy in seeking protection against acts ultra vires of the corporation, was expressed by Sir John Romilly, master of the rolls, in *Gregory v. Patchett*, 33 Beav. 595, 602, in this form: "Shareholders cannot lie by, sanctioning, or by their silence at least acquiescing in an arrangement which is ultra vires of the company to which they belong, watching the result; if it be favorable and profitable to themselves to abide by it and insist on its validity; but if it prove unfavorable and disastrous then to institute proceedings to set it aside." and Lord-Justice Turner's statement of the rule is equally pertinent to the case in hand. In *Great Western Ry. Co. v. Oxford, Worcester & Wolverhampton Ry. Co.*, 3 De G., M. & G. 341, 359, he said: "Where the summary interference of this court is invoked, in cases of this nature, it must be invoked promptly. Parties who have lain by and permitted a large expenditure to be made, in contravention of the rights for which they contend, cannot call upon the court for its summary interference. The jurisdiction to interfere is purely equitable, and it must be governed by equitable principles. One of the first of those principles is that parties coming into equity must do equity; and this principle more than reaches to cases of this description. If parties cannot come into equity without submitting to do equity, a fortiori they cannot come for the summary interference of the court when their conduct before coming has been such as to prevent equity being done." The cases in which this principle, as it is applied to stockholders, has been discussed, are numerous. The doctrine they establish is, that where an act is done openly, and especially on notice, and without evil intent, though clearly in excess of the power of the corporation, a non-assenting stockholder will not be allowed to pause to speculate upon the chances—to wait until he can see whether such act is likely to result in profit or loss—but to be entitled to the summary interference of the court he must ask for it promptly, and before the act of which he complains has become the foundation of rights or equities which must be destroyed or greatly impaired if the act be nullified or undone. Or, stated with greater brevity, and in its simple essence, the rule is this: If he wants protection against the consequences of an ultra vires act he must ask for it with sufficient promptness to enable the court to do justice to him without doing injustice to others. *Kent v. Quicksilver Mining Co.*, 78 N. Y. 159; *Sheldon Hat Blocking Co. v. Eickemeyer Hat Blocking Co.*, 90 N. Y. 607; *Watt's Appeal*, 78 Pa. St. 370; *Kitchen v. St. Louis, Kansas City & Northern R. R. Co.*, 69 Mo. 224; *Taylor v. South & North Alabama R. R. Co.* 4 Wood (U. S.) 575; *Graham v.*

Birkenhead, Lancashire & Cheshire Junction R. R. Co., 2 Man. & G. 146.

This principle must control the decision of the present application. No argument is required to show its pertinency. When the leading facts of the case are recalled it applies itself. Whether the complainants remained inactive to speculate upon the chances, intending to abide by the consolidation if it resulted in benefit, and, if not, to try to undo it, it is manifest that they acted precisely as they would have done if such had been their intention. Although they were fully informed of each step in the consolidation scheme from its inception to its completion, and also of the fact that the new corporation had been organized and was actively engaged in the prosecution of the several enterprises which had previously been carried on by the four corporations separately, yet, for over three years, they remained passive and inactive and did nothing, and it is not until the new corporation has become insolvent, and all of its property is about to be sold to pay mortgages, which were made and accepted while they were apparently assenting to the amalgamation and all its consequences, that they seek to have the consolidation broken up and the property of the corporation in which they are interested restored to it. They laid by until the new venture proved disastrous, and then, for the first time, they ask the court to undo what for over three years they had, by their inaction and delay, been apparently assenting to. Acquiescence or tacit assent, in such cases, was defined by Judge Folger in *Kent v. Quicksilver Mining Co.*, *supra*, to mean neglect to promptly and actively condemn the unauthorized act by suit. More than a year elapsed between the formation of the new corporation and the execution of the four mortgages to the defendant. If the validity of the new corporation had been promptly challenged by suit, it is almost absolutely certain that the debts secured by those mortgages would not have been contracted. Neither the mortgages nor the debts would have then existed. As it is, those mortgages are unquestionably good and valid as against the assenting stockholders. It is probable that two hundred and thirty-seven out of the two hundred and forty-nine shares have assented. It is certain that one hundred and eighty-four have. In this situation of affairs, it is obvious, to arrest the defendant's foreclosure suit will prevent him, at least for the present, from enforcing that part of his security which is good beyond question, and this must be done, if done at all, to protect the complainants in the enjoyment of a right, small in both extent and value compared with that of the defendant, and which it is not at all certain they have not irretrievably lost by their laches. The complainants, in my judgment, occupy the position described by Lord-Justice Turner when he said: "Suitors cannot come for the summary interference of the court when their conduct, before coming, has been such as to prevent equity being done." The complainants' application will be denied, with costs.¹¹

¹¹ *Levin v. Chicago etc. Coke Co.* (1896) 64 Ill. App. 393; *Sheldon Hat*

TOWERS v. AFRICAN TUG CO.

1904. L. R. (1904) 1 Ch. Div. 558.¹²

THIS was a suit by two stockholders on behalf of themselves and all the other stockholders of the company, against the company and its directors, to compel the directors to repay to the company the amount of the dividend paid out of capital.

VAUGHAN WILLIAMS, L. J.—On the whole I do not think the plaintiffs are entitled to any relief. * * *

In that state of things, what ought to be done with this action? There is no doubt that the payment of this interim dividend was an ultra vires payment. [I start with the assumption one is bound to make, that if an act is done by a company which is ultra vires, no confirmation by shareholders—not even by every member of the company—can convert that which was ultra vires into something intra vires: it always must be ultra vires.] As is pointed out in one or two of the cases, the result of that is that if the company are plaintiffs, no amount of acquiescence or resolutions by the shareholders can form an answer to the action by the company for the reinstatement of things in the position in which they would have been but for the ultra vires act complained of. But, to my mind, it is a different thing where the action is brought by a shareholder on behalf of himself and other shareholders. I am assuming this case to be one of

Blocking Co. v. Eickemeyer Hat Blocking Mach. Co. (1882) 90 N. Y. 607, 64 How. Prac. 467, *Accord*.

See also Alexander v. Searcy (1888) 81 Ga. 536, 8 S. E. 630, 12 Am. St. 337 ("stockholder, who has acquiesced for fifteen years, and who has received money from the corporation by reason of the illegal act" prevented "from taking advantage of its invalidity"); City of Chicago v. Cameron (1887) 120 Ill. 447, 11 N. E. 899 (no laches though delay of 11½ years); Von Arnim v. American Tube-Works (1905) 188 Mass. 515, 518, 74 N. E. 680 (delay excusable where minority stockholder kept in ignorance); Moore v. Silver Valley Min. Co. (1889) 104 N. Car. 534, 546, 10 S. E. 679 (gross delay "suggestive of a want of good faith"); Rothchild v. Memphis & C. R. Co. (1902) 113 Fed. 476, 51 C. C. A. 310 (delay of 17 months barred suit); Kessler v. Ensley Co. (1903) 123 Fed. 546, 567; Burrows v. Interborough Metropolitan Co. (1907) 156 Fed. 389 (no laches, delay due to stockholders' awaiting opinion of Attorney-General as to legality of transaction). Cf. Memphis & Charleston R. R. Co. v. Grayson (1889) 88 Ala. 572, 7 So. 122.

In Montgomery Light Co. v. Lahey (1898) 121 Ala. 131, 25 So. 1006, Dowdell, J., said (p. 137):

"Mere delay in the assertion of a right, without more, does not in itself constitute laches. * * * The doctrine of laches when not applied by analogy to some statute creating a bar, or upon the theory of a stale demand, must rest upon the doctrine of estoppel where rights have arisen upon presumed acquiescence from unreasonable delay. * * * When called upon to account by the corporation, or by the shareholder when he is authorized to maintain suit in his own name, the unfaithful director cannot cover his *mala fides* with the plea of laches, on account of mere delay in calling him to account."

It was *held*, also, in this case that after refusal by directors, the shareholder must seek redress through the stockholders.—Eds.

¹² Statement abridged. Portions of opinions omitted.—Eds.

those in which the facts have been such that an individual shareholder ought to be able to sue in a representative action for the purpose of preventing acts being done in reference to the company in which the shareholders are interested, and which might damnify the company by reason of those acts being ultra vires. I assume that an action not only to prevent ultra vires acts in the future but also to remedy acts that have been done ultra vires is an action which can be brought in the form in which this action is brought. But although that is so, my own opinion is that this is a kind of action which has to be brought by a plaintiff personally. It is an action which he cannot bring unless he has an interest; it is an action which a stranger could not bring.

Under those circumstances, what is it we have to ask ourselves here? If it be the fact, as I think it is, that these plaintiffs knew of all that had been done, received their dividends with knowledge of all the facts, and then brought this action with the money still in their pockets, ought they to be allowed to bring this action, which, as I have pointed out, is, to my mind, an action such as they can bring in consequence of their personal interest in the matter? I think not. I think that an action cannot be brought by an individual shareholder complaining of an act which is ultra vires if he himself has in his pocket at the time he brings the action some of the proceeds of that very ultra vires act. Nor, in my opinion, does it alter matters that he represents himself as suing on behalf of himself and others. I think that the reason which requires us to say he ought not to bring such an action equally requires us to say that he ought not to be the peg upon which such an action is to be hung for the benefit of others.

Assuming that to be so, what answer is sought to be made here? I think Mr. Evans was disposed to put the only logical answer that could be put, and to say he was bound to contend that the very wrongdoer himself, who had the proceeds of the wrong-doing in his own pocket, might, if the matter was one which was ultra vires, sue as a plaintiff to have it put right, and might bring his action against the other shareholders who had benefited by it to compel them to restore the capital which had been wrongfully paid out to them. But I do not think that is right; and if it is not right, I think that even the return of the capital after the action has been brought and before the trial does not make things any better. Admittedly, these dividends were still in the pockets of these plaintiffs when they brought this action; they were still in their pockets when the action came to be tried. It is quite true that in the course of the trial they said they were prepared to pay this money back, and in the result they were content that judgment should go against them personally in respect of it; but I do not think that would make an action good which was not otherwise a good action in its inception.

I must say in this particular case there is a strong inclination in my mind not to give the plaintiffs the relief which they ask, because, starting with the fact that capital had been disturbed in the

payment of this interim dividend, that fact had been recognized by the company and by the shareholders; it appears on the face of the balance-sheet, and they were minded to replace this capital, and had every prospect of completely replacing it of the profits of the very year in which this action was brought.

Under those circumstances this action was wholly unnecessary and wholly uncalled for. It seems to me the court is not bound, when it sees that this ultra vires act is in course of being put right, and will very shortly be put right, to give relief to a plaintiff who has acquiesced in the wrongs, and who himself has part of the proceeds of the wrong in his pocket. Under those circumstances I think this appeal ought to succeed.

STIRLING, L. J.—* * * Now the action is one by the plaintiffs on behalf of themselves and all other shareholders against the company; originally all the shareholders were not made parties, but the other shareholders were afterwards, at their own request, made defendants, so that now we have here all the shareholders of the company. I think this is a form of action which in certain circumstances may be maintained. That a shareholder who had received a dividend, without knowing anything of the illegality of it, might maintain such an action I do not doubt. Whether in some circumstances a shareholder so suing ought not to return what he had received in respect of dividend is another question. Why is it that this form of action is allowed? Prima facie the proper plaintiff, where it is sought to bring back the property of the company into its own coffers, is the company itself. But there are exceptions to that rule; and what is the reason of the exception? Sir George Jessel, in the case which has been referred to of *Russell v. Wakefield Waterworks Co.*, (1) says this: "The exceptions turn very much on the necessity of the case; that is, for the Court doing justice." Now this is a case in which, to begin with, no one suggests any fraud or dishonesty on the part of the directors or any one else. The directors who paid the dividend made a mistake, but no one charges them with anything more than a mistake. Everything was perfectly open. The fact was disclosed by the balance-sheet of 1900, the first balance-sheet which was submitted to the shareholders after the payment of the dividend. Further, the subsequent dealings seem to shew that the company did not intend to overlook the fact that this dividend had been improperly paid, or that there was an intention on the part of any one to do anything other than what was right, by making good the deficiency in the capital of the company which had been created by the payment of that dividend. That seems to me to have been the result of the subsequent balance-sheets. Moreover, what do we find the plaintiffs themselves doing? They acquiesce in this course being taken by the company from September 14, 1900, when they certainly knew it, down to March 20, 1903, when this action was brought. It does not seem to have ever been suggested

(1) L. R. 20 Eq. 480.

by any one that an action should be brought by the company to recover the deficiency of the capital; and I think we ought to infer that what commended itself to the plaintiffs, as well as to the other shareholders, was to go on in this way; the company was prosperous, it was wiping out year by year a great part of the deficiency, and the intention was ultimately, when the whole deficiency, including the deficiency in capital, had been replaced, to pay a proper dividend, and not until then. I do not think there was any necessity shown, looking at all the circumstances of the case, for the intervention of the Court to compel the payment of this small sum—for such it really was—in the way the plaintiffs seek. In truth, BYRNE, J., although he gave a judgment in favor of the plaintiffs, was so far from desiring to press it, that he directed it not to be enforced, in order to see what might be the result of the further trading, and whether the deficiency in capital would not be wiped out in the ordinary course.

I think, on the whole, that justice would have been done if this action had been dismissed on the ground that the personal conduct of the plaintiffs was such as to preclude them from insisting on the relief which they claim.

COZENS-HARDY, L. J.—I am of the same opinion. In my view there is one point here which really admits of no argument, namely, that this was an illegal payment as being a payment out of capital. Nor do I think that it can be contested—and it certainly was not contested by Mr. Eve—that a transaction of that kind cannot be ratified by the shareholders. But, in order to consider what is relevant in this case, one must go further. An action in respect of or arising out of an ultra vires transaction ought properly to be brought by the company; but it has long been well established that there are cases in which such an action may be maintained by a shareholder suing on behalf of himself and all other shareholders against the company as defendants. I will not pause to consider under what particular circumstances such an action may be maintained, but I assume that this is one of those cases in which such an action may be maintained—I mean in point of form. But I think it is equally clear that the action cannot be maintained by a common informer. A plaintiff in an action in this form must be a person who is really interested. When you get that fact clearly established it seems to me impossible to avoid taking the next step—that all personal objections against the individual plaintiff must be gone into and considered before relief can be granted. Here I think it is clearly proved, as it is certainly to be treated as admitted by the absence of any denial of the allegations in the counter-claim, that both the plaintiffs took this dividend with full notice of all the facts relating thereto. It is also clear that they had their dividends, which they took with full notice that they were payments out of capital, in their pockets at the date this action was commenced.

Now, can a shareholder who has, with full notice of all the mate-

rial facts, received part of the capital by way of a dividend, and who still retains that money in his pocket, maintain an action against the directors who have paid the dividend? I think the true answer to that question is, He cannot. It may be that there is no direct authority on the point; but the dictum of Brett L. J. in *Flitcroft's Case* (2) is very nearly in point. That was the case of the winding-up of a company: it was a case where there had been an illegal payment of capital; and what Brett L. J. says is this: "I think there was no ratification at all, because the assent of the shareholders was procured by improper accounts, the untruthfulness of which the shareholders did not know. But suppose they had known it, I think that what was done was a breach of trust which they could not ratify. If they had with full knowledge assumed to ratify what was done, they could not individually have complained, but the shareholders are not the corporation."

The view of Brett L. J. was that shareholders who assumed to ratify could not have individually complained, and it seems to me to follow that a shareholder, having the money in his pocket which he knows is wrongfully there, ought not to be allowed to complain; and he cannot get any greater right of complaint because his action is, in form, an action by himself and all the other shareholders in the company. In fact, he must succeed by his own merits and not by the merits of the other shareholders. Whether this action could have been maintained by these plaintiffs if, before action brought, they had repaid the amount of the dividend which they had received, it is not necessary for us to decide. Speaking for myself, I doubt whether that payment could have sufficed to put the plaintiffs in the right. Here, however, nothing of the kind happened: there is actually a judgment against the plaintiffs upon the counter-claim for the payment of these sums.

In my view the judgment of the learned judge in the action ought to be set aside, the judgment on the counter-claim, with costs, being the only part of the order which can stand.¹⁸

HILL v. MURPHY.

1912. 212 Mass. 1, 98 N. E. 781.

BILL IN EQUITY, filed in the Supreme Judicial Court on June 16, 1911, by certain stockholders of the Eastern Cold Storage Company, a corporation, against the directors of that corporation, the corpora-

(2) 21 Ch. D. 519, 534-5.

Accord, *Wormser v. Metropolitan Street R. Co.* (1906) 184 N. Y. 83. 76 N. E. 1036, 112 Am. St. 596. See also *De Bussche v. Alt* (1878) L. R. 8 Ch. Div. 286, discussing "acquiescence," p. 314 *et seq.*

It is a defense to show that the complaining shareholder is suing simply as the puppet of a rival corporation, *Forrest v. Manchester &c. R. Co.* (1861)

Nov. 23-1915- Cuit. from 688-697.

*after 698
Cuit. to 704
Cuit. 710-722
Read first 6 cases - section 8.*

tion and its treasurer, containing the allegations which are stated in the opinion.

All the defendants demurred to the bill. They also filed an answer. The case came on to be heard before Morton, J. who reserved it upon the bill, the demurrer, the answer and an agreed statement of facts for determination by the full court.

DECOURCY, J.—It must be assumed, for the purpose of the demurrer, that the following facts alleged in the bill are true. The defendants, Murphy, Musgrave, Simonds, Jones and Mason, as directors of the Eastern Cold Storage Company and in its name, published a false and malicious libel of and concerning one Walter L. Hill in connection with his official acts as treasurer and director of the company. Hill brought an action against the corporation for the libel and recovered judgment for a substantial amount; and this sum, together with the expenses incurred in defending the action, was paid by the defendants out of the treasury of the corporation. It is further alleged that the publication of the libel was wholly outside the legitimate business of the Eastern Cold Storage Company, that it was maliciously circulated by the defendant directors to injure the plaintiff and to gratify their own personal ends, and that demand was made upon them to reimburse the corporation.

Clearly the bill sets out a cause of action in favor of the corporation against the defendant directors. When directors intentionally act ultra vires of the corporation, they are liable for the losses it sustains in consequence. *Richardson v. Clinton Wall Trunk Co.* 181 Mass. 580, 64 N. E. 400; *Greenfield Savings Bank v. Abercrombie*, 211 Mass. 252, 97 N. E. 897, and cases cited. *Leeds Estate, Building & Loan Association v. Shepherd*, 36 Ch. D. 787; *Williams v. McDonald*, 42 N. J. Eq. 392, 7 Atl. 866. And regardless of whether the publishing of the libel was within the powers of the corporation the tortious act, alleged to be wilfully done by the directors to gratify their own personal ends, was a breach of the duty they owed as quasi trustees and it has resulted in loss to the corporation.

. . . The liability of directors is not limited to cases where the loss to the corporation results from fraudulent misconduct on their part, or where they have received financial profit which in equity belongs to the company. *Von Arnim v. American Tube Works*, 188 Mass. 515, 74 N. E. 680; *Greenfield Savings Bank v. Simons*, 133 Mass. 415. And the familiar decisions of non-liability of directors acting honestly and within their powers for losses sustained by the corporation through their negligence, do not apply. *Lyman v. Bonney*, 118 Mass. 222; *Overend, Gurney & Co. v. Gibb*, L. R. 5 H. L. 480; *Hun v. Cary*, 82 N. Y. 65, 37 Am. Rep. 546; *Savings Bank*

4 De G. F. & J. 125, 30 Beav. 40; *Beshoar v. Chappell* (1895) 6 Colo. App. 323, 40 Pac. 244; *Breeze v. Lone & Co. Mining Co.* (1905) 39 Wash. 602, 81 Pac. 1050. Otherwise, however, where complainant sues *bona fide* in his own interest and merely his motives are questionable. *Seaton v. Grant* (1867) L. R. 2 Ch. App. 459; *Hodge v. U. S. Steel Corporation* (1902) 64 N. J. Eq. 111, 53 Atl. 553, rev'd., 64 N. J. Eq. 807, 54 Atl. 1.—Eds.

of *Louisville v. Caperton*, 87 Ky. 306, 8 S. W. 885, 12 Am. St. 488. See *Phoenix Ins. Co. v. Frissell*, 142 Mass. 513, 8 N. E. 348.

This liability ordinarily would be enforced in an action at law by the corporation, but where those in control refuse to act the minority stockholders may bring a bill in equity in behalf of and for the benefit of the corporation. The allegations in the bill, while somewhat meagre, fairly bring the case within the rule where the plaintiffs have no remedy within the corporation. *Brewer v. Boston Theatre*, 104 Mass. 378; *Dunphy v. Traveller Newspaper Association*, 146 Mass. 495, 16 N. E. 426.

It is conceded that if a case is stated against the directors then the corporation is a proper party. As to the defendant directors and the corporation the demurrer must be overruled.

But the demurrer of the defendant Smith must be sustained. He was not concerned in publishing the alleged libel, and did only his duty as treasurer in paying the execution against the corporation. The allegation that demand was made upon him to proceed "in accordance with the by-laws of said corporation" to collect from the directors the sums expended in paying the judgment and expenses is insufficient without setting out by-laws that authorize such proceedings by the treasurer.

Upon the issues raised by the bill and answer, the allegations in the answer are controlled by the agreed statement of facts. *Taunton v. Taylor*, 116 Mass. 254. The admission that "it is useless for the plaintiffs to seek for the relief sought for in their bill by any action within the corporation" establishes the right of the plaintiffs to recover if the Eastern Cold Storage Company itself could maintain the action; and the demand admittedly made upon the defendant directors to reimburse the corporation appears to be sufficient, if demand was necessary. The defendants seek hereby to raise two questions in addition to those resulting from the demurrer. The first is that in publishing the circular letter the defendant directors were protected by the law of privileged communications. Without conceding that this question is open in an action by the corporation for reimbursement, it is not supported by the answer or agreed facts. Aside from the general denial in the answer that the defendants published a false and malicious libel, it is not stated that the circular, which it is agreed was signed and published by them, was in the performance of any duty or in good faith, without actual malice; nor is there any denial of the allegations that the publication was wholly outside the legitimate business of the corporation, and was issued to gratify the personal ends of the directors.

The other defense argued is that the defendants were sued individually by said Hill for the same libel, and recovered judgment. The record in the two actions brought by Hill is not before us. Presumably the corporation was held answerable because the libel was published by its agents in the course of their business. *Fogg v. Boston & Lowell Railroad*, 148 Mass. 513, 20 N. E. 109, 12 Am. St.

583. And while the plaintiff could recover against either the principal or agents he could not look to both where the tort complained of was not their joint act. *Parsons v. Winchell*, 5 Cush. 592, 52 Am. Dec. 745; *Mulchey v. Methodist Religious Society*, 125 Mass. 487. But whatever the explanation the issues and parties were different, and the judgment in the former action is not a bar to recovery in the present one. In that proceeding the question was whether the defendants were individually liable to Hill; in the present one the corporation seeks indemnity for the damages it suffered due to the misuse of their powers by the defendants while acting as its directors.

A decree for the plaintiff is to be entered; its form and details to be settled before a single justice.

So ordered.

HEARST v. PUTNAM MINING CO.

1904. 28 Utah 184, 77 Pac. 753.¹⁴

THIS is an action in equity resulting from certain mining transactions whereby the plaintiffs, shareholders in the Putnam Mining Company, claim that they were defrauded. The answer contained a general denial and pleaded as a separate affirmative defense, and as a bar to the action, that heretofore Margaretta V. Rogers, one of the shareholders of the Putnam Mining Company, prosecuted, in the right and for the benefit of the corporation, a suit to set aside and annul the sale and transfer of the property of the Putnam Company for the same alleged grounds and the identical dealings and transactions which are alleged and set forth in the complaint herein; that, in said action, the Putnam Mining Company and the Quincy Mining Company were made parties defendant, and, as such, appeared in that action, and that, upon the trial thereof, it was adjudged that neither Mrs. Rogers nor the Putnam Mining Company was entitled to an accounting, nor to any relief on account of the alleged dealings, because the same were in all respects fair and just; that the judgment was entered accordingly, and that the same is now a valid and subsisting judgment. The trial court dismissed the complaint and plaintiffs appeal.

BARTCH, J. (after stating the facts).—The decisive question presented in this case is whether the court erred in overruling the demurrer to the special and separate defense set up in the answer, and in denying the motion to strike out that portion of the answer.

The appellants contend that the judgment in the case of *Rogers v. Ferry et al.*, wherein the Putnam Mining Company was made a defendant, constitutes no bar to this suit, and that their demurrer should have been sustained and their motion granted.

¹⁴ Statement abridged. Portions of opinion omitted.—Eds.

The respondents insist not only that this action is barred by the judgment in the Rogers Case, but also that these plaintiffs must fail because they have brought and are attempting to maintain this suit in their own right, and not in the right of the Putnam Mining Company, although they claim only as stockholders of the corporation. The position of the respondents seem to be sound. And first as to the suit having been brought for the benefit of the plaintiffs, in their own right, and not that of the Putnam Mining Company: In their complaint the plaintiffs allege the corporate existence of the Putnam Mining Company; that they are stockholders of the corporation; that the corporation owned and operated certain mining property; that, through certain fraudulent dealings and transactions, the directors and agents of the company conveyed all its property to Ferry and his associates; and that, although the property has since been very productive, and has paid large sums in dividends, no accounting has been made to the plaintiffs, nor to the Putnam Mining Company. They then demand that the alleged fraudulent dealings and transactions be set aside, and the instruments of conveyance decreed null and void; that an accounting be had of all the money and stocks received by or due the vendee; that the just proportion to be paid the plaintiffs be ascertained; and that judgment be entered in their favor for the amount found due them. They then ask "for such further or all other relief as plaintiffs may be entitled to in equity and good conscience." They thus sue in their own right and for their own benefit only, notwithstanding the general allegation that the suit is also for the benefit of others who are in like situation, and who may appear as parties. They appear to proceed upon the theory that, because of the alleged fraudulent transactions, they are cestuis que trustent of a constructive trust, or a trust created in their favor, *ex maleficio*, by wrongful acts of the defendants, in dealing with the property and assets of the Putnam Mining Company. Under the facts disclosed by this complainant, no suit can be maintained upon such a theory. As has been seen, the allegations of the complaint clearly show that all the property in controversy was owned by and belonged to the corporation, and not to the plaintiffs, and it is not disputed that the corporation could own and hold its corporate property in absolute right, the same as an individual. Nor can it be, for a corporation is a distinct entity, an artificial person, created by law, and, as such, in this State, is capable of suing and being sued, of acquiring, owning, and disposing of property, within the objects of its creation, the same as a natural person; and one may deal with it, respecting its property, the same as with an individual owner, and without any greater danger of being held to have received property into his possession burdened with a direct trust or lien. Being a creature of statute, and having conferred upon it its individuality by law, which has endowed it with a legal existence, independent of any or all of its stockholders, the corporation has the

same dominion over its corporate property, with the same right of disposition, as a private person has over his.

* * * * *

Since, then, the corporation was capable of owning, and in fact did own, the property in controversy, absolutely, as a distinct entity, how could that property be held to be property in trust for the benefit of persons who are admittedly not the owners thereof, and who have, at most, but an interest in the fund created by the operation or disposition of the property? The very fact that the plaintiffs were not the owners of the property in dispute precludes the idea of a trust having arisen in their favor, *ex maleficio* or otherwise, for in the existence of every trust there are three essential elements, the absence of any one of which is fatal to the trust. These are a trustee, a beneficiary or cestui que trust, and property belonging to the cestui que trust. Here the property proposed to be impressed with a trust does not belong to the plaintiffs, and, as to them, is not in trust, they having but an indirect interest therein; and neither the plaintiffs nor any other stockholders have any interest or estate in the property, legal or equitable, which they can enforce in their own right and for their own special benefit. Nor is there any trust relation which enables a stockholder to sue in such a case. "The relation of trustee and cestui que trust, or of debtor and creditor or of partnership, does not exist between the stockholders of an incorporated company and the corporation itself. But the corporation and the individual shareholder may deal with each other at arm's length, the same as two strangers may, and a shareholder may contract with his corporation, and sue and be sued on his contracts." 1 *Thomp. Corp.* § 1076.

If a right of action exists, because of the alleged fraudulent acts and dealings in relation to the property in controversy, it exists in favor of the corporation, and of necessity the action must be brought in the right of the corporation, and for its benefit. If the defendants must account to any one for the property in litigation, the accounting must be to the corporation, and not to the plaintiffs or any other stockholders. The prayer of this complaint, in effect, asks the court to adjudge that the defendants have obtained for themselves, through fraudulent acts and dealings, the property of the corporation, and, instead of asking that the property so obtained, or its proceeds, be returned to the rightful owner, demands that the plaintiffs, for their own benefit, be decreed a portion of the fruits of the fraud. In other words, according to their prayer, they seek to obtain a portion of the property and assets of a third party, which they say was obtained from such third party by fraud. That a stockholder of a corporation cannot recover corporate property, fraudulently or otherwise disposed of by the officers or agents of the corporation, by suing in his own right and for his own benefit, is settled by the authorities. It is true, where the property or assets of a corporation have been sequestered and dissipated by fraud or

otherwise, a stockholder may, if the board of directors will not act, and a suit clearly ought to be brought, sue in the right of the corporation to have its property restored to it, or to obtain for it such other relief as the circumstances may demand, but in no such case can he sue for himself in his own right. This right of a stockholder to sue, in cases of fraud, for the benefit of the corporation, when it will not sue, is an exception to the general rule "that actions to redress wrongs done to a corporation must be brought by the corporation itself, and that such actions cannot be brought by its stockholders." 4 Thomp., Corp. section 4488.

(The learned judge proceeded to discuss the authorities.)

* * * * *

There are instances, however, where a stockholder may apply to a court of equity for a preventive remedy by injunction to restrain those who are administering the affairs of the corporation from doing acts which are ultra vires, or to prevent a misapplication of the corporate funds which might result injuriously to the stockholders, where the acts intended to be performed would amount to a breach of trust. In such and like cases a preventive remedy may be applied at the instance of a stockholder, but such cases are wholly different from those like the one at bar.

Mr. Thompson, in his Commentaries on the Law of Corporations, vol. 4, § 4491, states the distinction thus: "Where an action is brought by one or more stockholders to enjoin the performance of ultra vires, fraudulent, or oppressive acts on the part of the directors, the remedy is preventive; consisting of an injunction against the performance of such acts, to which may be superadded, in appropriate cases, other forms of equitable relief. Where, on the other hand, the action is brought to undo frauds and breaches of trust already committed, and to restore to the corporation assets thereby wasted, the action does not, as in the former case, proceed in right of the stockholder, but it proceeds in right of the corporation, and consequently whatever is restored accrues to the corporation."

Where, then, as in this case, the acts complained of have been fully consummated, and the title to the property has passed into the hands of third parties, a stockholder has no remedy to recover, in his own right, any specific or proportionate part of the property for his own benefit. And where the corporate property of such a corporation, in whole or in part, has been sold or disposed of in good faith, under the powers of its charter, and not as a result of fraudulent purposes, the minority stockholder has no cause for complaint, for, as we have seen, a corporation of this character may, in the absence of restraint by the law of its creation, lease, sell, or dispose of any or all of its property, the same as an individual may do respecting his property. This may be done by a majority of the members. The principle that the majority must rule in the management of the affairs of a corporation "is rigidly upheld in equity, in the absence of fraud, oppression, and ultra vires acts." 4 Thomp., Corp.

§ 4533; 2 Kent, Com. 280-282; *Weyeth H. & M. Co. v. James-Spencer-Bateman Co.*, 15 Utah 110, 47 Pac. 604; *Ardesco Oil Co. v. N. A. Min. & Oil Co.*, 66 Pa. 375; *Treadwell v. Salisbury Mfg. Co.*, 7 Gray 393, 66 Am. Dec. 490; *Central Transp. Co. v. Pullman's Car Co.*, 139 U. S. 24, 50, 11 Sup. Ct. 478, 35 L. ed. 55; *Twin-Lick Oil Co. v. Marbury*, 91 U. S. 587, 23 L. ed. 328.

But suppose this suit were regarded and treated as brought, not in right of the plaintiffs nor for their own benefit, but in right of all the stockholders, and hence for the corporation, and for its benefit; then could the plaintiffs recover? We think not, because, reviewing this suit in that light, they are met at the very threshold with the judgment in the case of *Rogers v. Ferry et al.*, where the Putnam Mining Company was a defendant, and which forms the special plea in the answer herein. The plaintiffs, by their demurrer to that plea, have admitted, for the purpose of this case, all the averments properly pleaded therein to be true. Among such averments, it appears that that suit was brought and tried in a district court of this State—a court of competent jurisdiction; that the plaintiffs therein sued in right of the corporation, the Putnam Mining Company; that the Putnam Mining Company and the Quincy Mining Company were there, same as here, parties defendant; that the identical cause of action and the identical matters which are herein charged as fraudulent were therein pleaded and tried; that court adjudged and determined that all the transactions and dealings complained of were lawful and made in good faith, and were without any fraud done or intended; and that neither the Putnam Mining Company, nor the plaintiff therein, was entitled to any accounting in respect of the matters charged in that complaint; and that such judgment is of record, and is still in full force and effect. Thus it clearly appears that the Rogers suit was brought and intended for the purpose of undoing the very transactions complained of in this action as being a fraud on the Putnam Mining Company and its stockholders, and the judgment was that neither the plaintiff nor the corporation was entitled to an accounting. As that suit was brought in the right of the corporation, that judgment is binding upon the corporation, and, by the rule of representation, all the stockholders are equally bound by it. It follows that, since the transactions and dealings complained of in that suit are exactly the same transactions and dealings complained of in this action, that judgment, being in full force and effect, is conclusive against the right of the plaintiffs to recover herein; they being stockholders in the corporation. The court having decided that there was no fraud in the transactions in controversy, and that the corporation has no right of recovery, no stockholder can make the same transactions the basis for complaint.

In *Hawkins v. Glenn*, 131 U. S. 319, 9 Sup. Ct. 739, 33 L. ed. 184, where the plaintiff in error, who was a stockholder, claimed that a certain order or decree which was binding upon the corporation was void, as against him, because he was not a party to the

suit in which the order was made, the Supreme Court of the United States held that, "in the absence of fraud, stockholders are bound by a decree against the corporation in respect to corporate matters, and such a decree is not open to collateral attack." Mr. Chief Justice Fuller, delivering the opinion of the court; said: "Sued after such an order of court, the defendant does not deny the existence of any one of the facts upon which the order was made, but contends that there has been no call, as to him, because he was not a party to the cause between creditor and corporation. We understand the rule to be otherwise, and that the stockholder is bound by a decree of a court of equity against the corporation in enforcement of a corporate duty, although not a party as an individual, but only through representation by the company. A stockholder is so far an integral part of the corporation that, in the view of the law, he is privy to the proceedings touching the body of which he is a member." Freeman on Judgments, §§ 176, 178; Glenn v. Williams, 60 Md. 93; Kessler v. Ensley Co. (C. C.), 123 Fed. 546.

The fact that this suit was brought by different parties plaintiff is immaterial, since these plaintiffs, as stockholders, were privy to the proceedings in the former suit, and since both suits were identical as to cause of action, subject-matter, purpose, and object, quality of persons for or against whom claim is made, and as to the thing adjudged. These legal identities existing, and the same questions involved herein having been judicially settled and determined in the Rogers suit, the judgment in that case is an effectual bar to this action. Freeman on Judgments, §§ 252, 253, et seq.; New Orleans v. Citizens' Bank, 167 U. S. 371, 17 Sup. Ct. 905, 42 L. ed. 202; Cromwell v. County of Sac, 94 U. S. 351, 24 L. ed. 681; Lyon v. Perin & Goff Manufacturing Co., 125 U. S. 698, 8 Sup. Ct. 1024, 31 L. ed. 839.

From the foregoing considerations, and the authorities, the conclusion is inevitable that the court did not err in overruling the demurrer or denying the motion directed at the special plea, nor in rendering judgment in favor of the defendants on the merits.

We find no reversible error in the record. The judgment is affirmed, with costs.

BASKIN, C. J., and McCARTY, J., concur.¹⁸

¹⁸ Willoughby v. Chicago Junction Railways &c. Co. (1892) 50 N. J. Eq. 656, 25 Atl. 277, *Accord*, the court saying, "If not so there can be no end of litigation, for the court is then open to suit by every stockholder, *seriatim*, presenting the questions over and over for consideration and decision."

See Montezuma Cattle Co. v. Dake (1901) 16 Colo. App. 139, 63 Pac. 1058.—Eds.

TOMKINSON v. SOUTH-EASTERN R. CO.

1887. L. R. 35 Ch. Div. 675.¹⁸

THIS was a motion by the plaintiff, a holder of £500 deferred ordinary stock of the South-Eastern Railway Company, for an injunction to restrain the company and its directors, officers, servants, and agents, until the trial of the action or further order, from subscribing, advancing or paying, out of the moneys of the company, the sum of £1000, or any other sum, by way of donation, or otherwise, to or for the purposes of the Imperial Institute, or to any person or persons on behalf of the Institute.

KAY, J.:—

I have no doubt that it is the duty of the Court to grant an injunction in this case.

The question, as the Attorney-General said, is whether the act proposed to be done is within the powers of the railway company, or outside its powers. If it is outside its powers, it is now perfectly settled that any one shareholder may come to this Court and say, "This company is going to do an act which is beyond its powers; stop it;" and the Court thereupon has no discretion in the matter.

Now, what is proposed to be done here is this: the chairman of the railway company, at a meeting of the company, proposed this resolution: "That the directors be authorized, either by way of donation from the company or by an appeal to the proprietors, as they may be advised"—the resolution thus proposing two alternative modes—"to subscribe the sum of £1000 to the Imperial Institute." I pause there. The Imperial Institute has no more connection with this railway company than the present exhibition of pictures at Burlington House, or the Grosvenor Gallery, or Madame Tussaud's, or any other institution in London that can be mentioned. The only ground for the suggestion that this company has the right to apply its funds, which it has been allowed to raise for specific purposes, to this purpose, is, that the Imperial Institute, if it succeeds, will very probably greatly increase the traffic of this company. If that is a good reason, then, as I pointed out during the argument, any possible kind of exhibition which, by being established in London, would probably increase the traffic of a railway company by inducing people to come up to see it, would be an object to which a railway company might subscribe part of its funds. I never heard of such a rule, and, as far as I understand the law, that clearly would not be a proper application of the moneys of a railway company. I cannot distinguish this case from that at all, though, of course, I do not mean to disparage the enormous importance of the Imperial Institute. It may be established for the highest possible objects of interest to this country; but still, the only reason given to me why this railway company thinks it right to spend part of its funds in

¹⁸ Statement abridged. Portion of opinion omitted.—Eds.

subscribing to it is this, that it will probably greatly increase the traffic of the company by inducing many people to travel up to visit this Institute. I cannot accept that as a reason for a moment. Therefore, as at present advised, it seems to me that this is *ultra vires*.

* * * * *

I know of no authority whatever for saying that the payment of £1000 out of the funds of this company as a subscription to the Imperial Institute would be within the powers of a railway company. I might stop there, because, this being an application for an interlocutory injunction, I am bound, if I felt difficulty upon the question, to restrain the matter until the trial of the action; but my present opinion is entirely against the validity of this act.

Therefore, it seems to me I am clearly bound to restrain, until the trial of this action, the expenditure of this money out of the company's funds.¹⁷

CONVERSE v. UNITED SHOE MACHINERY CO.

1904. 185 Mass. 422, 70 N. E. 444.

KNOWLTON, C. J.—This is an action at law brought against the defendant corporation and three other defendants, sued personally, for conspiring to injure and ruin another corporation, the Goddu Sons Metal Fastening Company, in which the plaintiff is a stockholder.

The averments of the declaration are, in substance, that the three personal defendants "conceived a plan of acquiring, by purchase or otherwise, the control of said Goddu Sons Metal Fastening Company and of absorbing its rights, patents and other property into the said United Shoe Machinery Company, of which they were

¹⁷ In *Hoole v. Great Western R. Co.* (1867) L. R. 3 Ch. App. Cas. 262, Lord Cairns, L. J., said: "I am anxious to do complete justice to the motives, so far as I can form an opinion upon them, which have led the company, and the executive of the company, and the general meetings, to suggest, and, as far as they could, to carry into effect, the arrangement that has been made. * * * I believe that it was an arrangement which all the parties to it believed to be most advantageous to the company, and to every person concerned; and, as far as it is proper to feel regret, one may feel regret that the arrangement did not meet with the unanimous assent of all the shareholders. With that, however, we have nothing here to do; if the arrangement which has been proposed is legal, is *intra vires*, the company, through their general meetings, have power to carry it into effect; if, on the other hand, it is *ultra vires*, if it is illegal, any member of the company may dissent from it, and has a right to appeal to this Court to be protected against its effects." (p. 268)

See also *American Ice & Industries Co. v. Crane* (1904) 142 Ala. 620, 39 So. 233 (unauthorized bond issue restrained at suit of a stockholder); *Ashton v. Dashaway Ass'n.* (1890) 84 Cal. 61, 22 Pac. 660, 23 Pac. 1091, 7 L. R. A. 809; *Byrne v. Schuyler Elec. Mfg. Co.* (1895) 65 Conn. 336, 31 Atl. 833, 28 L. R. A. 304; *Carson v. Iowa City Gaslight Co.* (1890) 80 Iowa 638, 45 N. W.

officers and directors," and that afterward, combining and conspiring with the defendant corporation to injure the property of the other corporation, they acquired a majority of the stock of this other corporation and elected themselves directors and officers thereof, and as such officers and directors were guilty of various misfeasances in the control and management of the corporation, greatly to the injury and damage thereof and of the plaintiff's share and interest therein.

Each of the defendants demurred to the declaration, and the case is before us on the plaintiff's appeal from a judgment for the defendant, founded on an order sustaining the demurrer. Numerous grounds of the demurrer are stated, several of which we need not consider.

The defendants contend that the declaration is vague and indefinite, and that it does not set forth with sufficient certainty the cause of action relied on. We will not stop to consider this part of the demurrer, for if it is overruled, there are other particulars in which the case stated fails to show a ground of recovery. All the wrongs done or intended, set out in the declaration, are wrongs against the corporation in which the plaintiff is a stockholder, and except through the corporation, they have no relation to the plaintiff. She was not affected by the defendants' conduct, except as every other stockholder was affected. Against her as an individual there was no conspiracy, and against her as an individual, no wrong was done directly. There is no direct legal privity between her individually or as a stockholder and these defendants. She has an interest in the corporation, and in the conduct of its officers affecting its property, but this interest in the transactions of the officers is not legal but equitable, and it cannot be made the foundation of an action at law against the officers. That an action at law cannot be maintained in a case of this kind was clearly shown by Chief Justice Shaw in *Smith v. Hurd*, 12 Metc. 371. The plaintiff must find her remedy for such a wrong through a suit by the corporation or through a bill in equity, if she is unable to induce action of the corporation or its officers for the benefit of the stockholders. *Peabody v. Flint*, 6 Allen 52; *Brewer v. Boston Theatre Company*, 104 Mass. 378; *Dunphy v. Traveller Newspaper Association*, 146 Mass. 495; *Richardson v. Clinton Wall Trunk Manuf. Co.*, 181 Mass. 580; *Allen v. Curtis*, 26 Conn. 456; *Conway v. Halsey*, 15 Vroom 462; *Ritchie v. McMullen*, 79 Fed. 522.

The averment of conspiracy adds nothing, in legal effect to the

1068; *Shaw v. Staight* (1909) 107 Minn. 152, 119 N. W. 951, 20 L. R. A. (N. S.) 1077; *Theis v. Durr* (1905) 125 Wis. 651, 104 N. W. 985, 1 L. R. A. (N. S.) 571 (unauthorized release of subscription contract). Cf. *Russell v. American Gas & Elec. Co.* (1912) 136 N. Y. S. 602.

As to the distinction between a suit in the stockholder's individual right and in the corporate right, see also *Alexander v. Atlanta &c. R. Co.* (1901) 113 Ga. 193, 38 S. E. 772, 54 L. R. A. 305; *Witherbee v. Bowles* (1911) 201 N. Y. 427, 95 N. E. 27.—Eds.

other averments of the declaration. *Parker v. Huntington*, 2 Gray 124-127; *May v. Wood*, 172 Mass. 11.

Judgment affirmed.

CONVERSE v. UNITED SHOE MACHINERY CO.

1911. 209 Mass. 539, 95 N. E. 929.

MORTON, J.—This is a bill in equity to compel the Shoe Machinery Company and the individual defendants to account for alleged wrongdoing as stockholders in and officers and directors of the Goddu Sons Metal Fastening Company, in the management and conduct of the business and property of said company. The Goddu Company is made a party defendant. The defendants severally demurred, and the case was thereupon reserved for the full court; if the demurrers are sustained the bill is to be dismissed; if overruled the case is to be remanded to the Superior Court and the defendants are to answer and such other proceedings are to be had as equity may require.

Without reciting the allegations of the bill it is plain, we think, that the bill sets out a wilful breach of duty on the part of the individual defendants as directors and officers of the Goddu Company, and an intentional violation and disregard by them of the obligations resting upon them as such officers and directors, and a sacrifice by them in combination with the United Shoe Machinery Company of the interests of the Goddu Company to promote those of the Shoe Machinery Company. The bill alleges that the plaintiffs have protested to the defendants against their acts and conduct as stockholders, officers and directors of the Goddu Company without avail; that the defendants own a large majority of the stock, and that any further application to them would be futile.

At or about the time that the bill in this suit was filed, an action at law was brought against these defendants based on substantially the same allegations. The defendants demurred and the demurrer was sustained by the full court. The case is reported in 185 Mass. 422.

The bill in the present case is not brought and does not purport to be brought, as we construe it, in behalf of the plaintiffs and such other stockholders as may join, or on behalf of the corporation, but is brought by the plaintiffs to enforce individual rights assumed to belong to them as stockholders, and this constitutes, it seems to us, as the case stands, a fatal defect and renders it necessary to sustain the demurrers. The wrong, if any, was done not to the plaintiffs as individual stockholders but to the corporation, and the remedy must be sought by or on behalf of the corporation. As was said by the present Chief Justice in the former case, "All the wrongs done or intended . . . are wrongs against the corporation . . . and ex-

cept through the corporation, they have no relation to the plaintiff." *Converse v. United Shoe Machinery Co.*, 185 Mass. 422, 423, and cases cited. In order to prevent a failure of justice stockholders are allowed to institute proceedings on behalf of the corporation if neither the corporation nor its officers can be induced to take action. But such proceedings derive their validity not from wrongs done to the individual stockholders instituting them but from the right of the stockholders to act under the circumstances on behalf of the corporation. When proceedings are instituted by stockholders in behalf of the corporation, it is necessary that the corporation should be made a party defendant, but we do not think that the fact that the corporation is made a party defendant is enough to show of itself that the proceedings in the present case are prosecuted in behalf of the corporation or of such stockholders as may join in the absence of any allegations in the bill to that effect. The whole tenor of the bill in the present case shows, we think, that it is brought for the purpose of enabling the plaintiffs to recover individually for damages alleged to have been suffered by them as stockholders in consequence of the wrongful conduct of the defendants as stockholders and officers of the Goddu Company in the management of its business. That, as we have said, cannot be done.

It sufficiently appears, we think, from the allegations of the bill that an attempt was made to procure redress through the corporation and its officers, and that any further attempt to obtain such redress would have been useless. We do not indeed understand the defendants to contend to the contrary. But for the reason that the bill does not appear to be brought on behalf of the corporation, or of such other stockholders, not defendants, as may join, which is in effect the same thing, and seeks to enforce individual rights against the defendants, the demurrers must be sustained and the bill dismissed.

*So ordered.*¹⁸

BIGELOW v. CALUMET, ETC., MINING CO.

1907. 155 Fed. 869.¹⁹

KNAPPEN, District Judge.—The complainant is a citizen of Massachusetts. The defendants, hereafter called, respectively, the Calumet & Hecla Company and the Osceola Company, are corporations

¹⁸ *Ames v. Amer. Telephone & Telegraph Co.* (1909) 166 Fed. 820, *Accord*. But see *Brown v. De Young* (1897) 167 Ill. 549, 47 N. E. 863; *Eaton v. Robinson* (1895) 19 R. I. 146, 31 Atl. 1058, 32 Atl. 339, 29 L. R. A. 100. Cf. *Rafferty v. Donnelly* (1900) 197 Pa. 423, 47 Atl. 202; *De Neufville v. New York & N. R. Co.* (1897) 81 Fed. 10, 26 C. C. A. 306.

In *Siegman v. Electric Vehicle Co.* (1905) 140 Fed. 117, (1907) 72 N. J. Eq. 403, 65 Atl. 910, *held* that a stockholder may bring suit on behalf of the corporation to recover from a director dividends illegally paid, although the directors and stockholders refused on demand to bring suit.—Eds.

¹⁹ Portions of opinion omitted.—Eds.

organized under the Michigan mining law, and engaged in the manufacture and sale of copper. The complainant, who is the president of and a substantial stockholder in, the Osceola Company, filed his bill on the 12th day of March, 1907, for the purpose of obtaining an injunction, both temporary and permanent, restraining the Calumet & Hecla Company from voting at the annual stockholders' meeting of the Osceola Company (then appointed to be held on March 14, 1907) a large block of the Osceola Company stock held by the Calumet & Hecla Company, as well as proxies for a large amount of other of such stock held by that company, upon the ground that the action of the Calumet & Hecla Company in buying and obtaining proxies for such stock constitutes an attempt to establish and maintain a monopoly of the business of mining, smelting, refining, and selling copper, contrary to the Sherman anti-trust act, the Michigan anti-monopoly law, and common-law obligations. Upon the filing of the bill, an order was issued restraining the voting of such stock in advance of the hearing of the application for temporary injunction, except to the extent of adjourning the annual meeting. Hearing upon the application for temporary injunction has been had upon the bill, answer, and testimony by way of ex parte affidavits filed on both sides.

* * * * *

It is contended that under the case made by the bill the grievance complained of is that of the Osceola Company, and that complainant, as a stockholder in that company, has not complied with general equity rule No. 94, adopted to prevent a collusive conferring of jurisdiction. The authorities agree that, where the relief is sought for the benefit of the corporation, the complaining stockholder must show that he has exhausted all means within his reach to induce the corporation to take action, to the extent of formally making demand for action upon the board of directors (and, as held in some cases, even upon the stockholders), unless it appears that such demand would be an idle ceremony. It is clear that such demand upon the stockholders would have been, in this case, an idle ceremony, as a majority of the stock is apparently controlled by the Calumet & Hecla Company. Moreover, but 22 days intervened between February 20th and March 14th, and the mining law required four weeks' publication of notice for special stockholders' meeting. 2 Comp. Laws Mich. 1897, § 6999. The bill alleges that the suit is not collusive; that the complainant had consulted with a majority of the directors, all of whom expressed their opinion that the corporation should not bring the suit, in view of the antagonism thereto on the part of the majority of the stockholders, and in view of the near expiration of their terms as directors. Assuming that the relief asked for belongs to the corporation, the question is: Does the bill show that demand upon the directors to bring the suit would be an idle ceremony? This hearing is not upon demurrer to the bill, but upon answer and affidavits. There is force in the suggestion that

the directors might properly be adverse to taking corporate action under the circumstances stated, and that under the allegations referred to there is as much ground for an inference that the board, if formally called together, would have declined to take corporate action, as in a case where individual directors are known to favor the situation complained of. The allegations *prima facie* negative collusion. If upon final hearing the jurisdiction of this court should be found to rest upon collusion, the bill would be then dismissed. The fact that the original bill did not allege compliance with rule 94 is not material. The amended bill was filed as a matter of right. On this hearing relief can be given on the amended bill with the same effect as if it were an original bill.

It is not clear, however, that the grievance complained of belongs solely to the corporation. An action at law for the recovery of damages on account of the acts sought to be enjoined would accrue to individual stockholders, under section 7 of the federal act and the eleventh section of the Michigan statute. *Metcalf v. American School Furn. Co.* (C. C.) 108 Fed. 909, 912; (C. C.) 122 Fed. 115, 116. The right of the complainant to maintain the bill for his personal interest is recognized by respectable authorities. *High on Injunctions* (4th Ed.), § 1227, and cases cited; *Dunbar v. American Tel. & Tel. Co.*, 224 Ill. 9, 79 N. E. 423. If the Osceola Company was not a necessary party, and the bill is maintainable upon general equity principles, this court would have jurisdiction through diversity of citizenship, and thus the case would not be within the mischief aimed at by the rule in question.

It is contended that the bill does not allege a threatened, direct injury to complainant from the proposed monopoly charged, beyond such injury as would be suffered by the general public, and that irreparable injury is not sufficiently alleged to justify injunction. The seventeenth paragraph of the bill alleges that if the Calumet & Hecla Company shall secure the intended control of the Osceola Company it will be able to, and will, control the Osceola Company in its own interests, and not in the interests of complainant and other stockholders similarly situated; that the officers of the Osceola Company will have no independence of action in the management of that company's affairs; and that thereby complainant and other stockholders will suffer great loss and damage. As before said, this hearing is not on demurrer to the bill. The paragraph in question must be construed in connection with the other paragraphs of the bill and the case presented upon this application. The bill alleges that the complainant is a director and officer of the Osceola Company, and defendant's affidavits allege that he receives a substantial salary. It is alleged that the Calumet & Hecla Company proposes to oust the present directors, including the complainant, as a director and officer. Complainant's affidavits tend to show that the Calumet & Hecla Company proposes to revolutionize the method of operation of the Osceola mine, both in mining, manufacturing, and selling, and in

the interuse of shafts, drifts, and openings, and that the proposed methods, if applied, will injure the value of complainant's stock. Surely injuries such as these are distinct from such as would be suffered by the general public through the creation of a monopoly, and are injurious not only to the corporation as an entity, but to the individual stockholders. Moreover, under the anti-trust laws, if an unlawful monopoly is created, the Osceola Company would be subject not only to fine, but to forfeiture of franchises, notwithstanding the monopoly is created by action of the stockholders rather than by corporate action. Clark & Marshall on Private Corporations, § 314 (R.) These injuries likewise are distinct from those suffered by the general public. If the injuries referred to shall be suffered by complainant, they are properly termed irreparable. High on Injunctions (4th Ed.) § 1227, and cases cited.

* * * * *

Upon these considerations, the issuing of temporary injunction in substantially the terms of the existing restraining order, which would operate to protect all interests concerned, seems both proper and expedient.

*Temporary injunction will issue accordingly.*²⁰

MENIER v. HOOPER'S TELEGRAPH WORKS.

1874. L. R. 9 Ch. App. Cas. 350.

THE bill in this case was filed by E. J. Menier, on behalf of himself and all the other shareholders of the European and South American Telegraph Company (except such of them as were defendants), against a company called Hooper's Telegraph Works, W. Hooper, H. W. Crace, and the European and South American Telegraph Company, and stated (amongst other things) as follows:—That the European Company was incorporated in 1871 with the object of carrying out an agreement between the plaintiff, Menier, and one Bradford, and others, for constructing a submarine telegraph from Europe to South America, under certain conventions and decrees of foreign governments. The capital of the company was to be £1,250,000 in 62,500 £20 shares, and by the articles of association provisions were made for holding meetings of the company, at which every member was to have one vote for every share held by him. That Hooper's Company were to make and lay down for the European Company telegraph cables from Portugal to Brazil. That a prospectus was issued and many shares were applied for, but

²⁰ Delavan v. N. Y. N. H. & H. R. Co. (1912) 137 N. Y. S. 207, reversed (1912) 139 N. Y. S. 17, two judges dissenting, *Accord*.

For later stages of the litigation in the principal case, see (1908) 167 Fed. 704, (1909) 167 Fed. 721.—Eds.

in consequence of objections raised the directors determined not to proceed with the allotment to the public, and the only shares allotted were 3,000 to Hooper's Company, 2,000 to the plaintiff, and 325 to thirteen persons, ten of whom were the directors. That £3 was paid on each of the shares so allotted. That one of the concessions for making the telegraph had been granted to the Baron de Maua, who was at one time chairman of the European Company, and this concession was claimed by the European Company. That a bill was filed in this court by the European Company against the Baron de Maua and another company, praying a declaration that the Baron de Maua was a trustee of the concession for the European Company, and that he might be restrained from transferring it to any one else. That a motion was made for an interlocutory injunction, and was refused by the Vice-Chancellor Malins, but on the balance of convenience only. That the European Company, and also Hooper's Company, at first intended to appeal against the order of the Vice-Chancellor Malins. That Hooper's Company afterward determined not to appeal, and then the directors of the European Company determined not to appeal, but to take steps for winding up the European Company. That the plaintiff was resident in Paris and ignorant of English law, and believed that any arrangements adopted by the directors would be for the benefit of the European Company, and not exclusively in the interests of Hooper's Company. That the plaintiff wished the appeal to proceed, and offered to bear the costs. That on the 12th of February, 1873, an extraordinary meeting of the European Company was held, at which a resolution was passed that the company be wound up voluntarily, and that the defendant Crace be the liquidator. That the resolution was proposed by one Kennedy, a director of Hooper's Company, and that Crace was secretary of Hooper's Company. That this resolution was confirmed at another extraordinary meeting, at which five persons only were present, of whom three were directors nominated by Hooper's Company, and one was Crace, the secretary. That the plaintiff protested against these proceedings. That the plaintiff was then ignorant, but had since discovered, that these proceedings took place through the influence of Hooper's Company. The bill then stated the circumstances of an arrangement between Hooper's Company and the Telegraph Construction and Maintenance Company and the Baron de Maua, under which it would be to the advantage of Hooper's Company that the agreement between them and the European Company should be put an end to, in order to benefit Baron de Maua's Company, and in order that Hoopers' Company might sell to another company the cable they were making for the European Company. That these arrangements were concealed from the plaintiff and the other shareholders in the European Company. That Hooper's Company procured the abandonment of the suit against the Baron de Maua, and the winding up of the European Company, through the influence which they had as holders of 3,000 shares in the European

Company, and through the influence of the directors nominated by them.

And the bill prayed that Hooper's Company might be declared not entitled to the benefit of the profits derived from the abandonment of the suit and other arrangements aforesaid, and might be declared a trustee of those profits for the plaintiff and the other shareholders in the European Company; and that the European Company and the defendants might be restrained from repaying to Hooper's Company any of the money paid on the allotment of shares in the European Company, and from disposing of the property of the European Company.

To this bill the defendants Hooper's Company and W. Hooper demurred for want of equity; and the defendants Crace and the European Company also demurred, and for cause of demurrer shewed that the plaintiff had not made out such a case as entitled him to recovery or relief.

The Vice-Chancellor Bacon, on the 12th of January, 1874, overruled both demurrers; and the defendants appealed.

SIR W. M. JAMES, L. J. :—

I am of opinion that the order of the Vice-Chancellor in this case is quite right.

The case made by the bill is very shortly this: The defendants, who have a majority of shares in the company, have made an arrangement by which they have dealt with matters affecting the whole company, the interest in which belongs to the minority as well as to the majority. They have dealt with them in consideration of their obtaining for themselves certain advantages. Hooper's Company have obtained certain advantages by dealing with something which was the property of the whole company. The minority of the shareholders, say in effect that the majority have divided the assets of the company, more or less, between themselves, to the exclusion of the minority. I think it would be a shocking thing if that could be done, because if so the majority might divide the whole assets of the company, and pass a resolution that everything must be given to them, and that the minority should have nothing to do with it. Assuming the case to be as alleged by the bill, then the majority have put something into their pockets at the expense of the minority. If so, it appears to me that the minority have a right to have their share of the benefits ascertained for them in the best way in which the court can do it, and given to them.

It is said, however, that this is not the right form of suit, because, according to the principles laid down in *Foss v. Harbottle* and other similar cases, the court ought to be very slow indeed in allowing a shareholder to file a bill, where the company is the proper plaintiff. This particular case seems to me precisely one of the exceptions referred to by Vice-Chancellor Wood in *Atwood v. Merryweather*, a case in which the majority were the defendants, the wrong-doers, who were alleged to have put the minority's prop-

erty into their pockets. In this case it is right and proper for a bill to be filed by one shareholder on behalf of himself and all the other shareholders.

Therefore the demurrer ought to be overruled.

SIR G. MELLISH, L. J.:—

I am entirely of the same opinion.

It so happens that Hooper's Company are the majority in this company, and a suit by this company was pending which might or might not turn out advantageous to this company. The plaintiff says that Hooper's Company being the majority, have procured that suit to be settled upon terms favourable to themselves, they getting a consideration for settling it in the shape of a profitable bargain for the laying of a cable. I am of opinion that although it may be quite true that the shareholders of a company may vote as they please, and for the purpose of their own interests, yet that the majority of shareholders cannot sell the assets of the company and keep the consideration, but must allow the minority to have their share of any consideration which may come to them. I also entirely agree that, under the circumstances, the suit is properly brought in the name of the plaintiff on behalf of himself and all the other shareholders.

*The appeal will be dismissed with costs.*²¹

PRICE v. HOLCOMB.

1893. 89 Iowa 123, 56 N. W. 407.²²

THE plaintiff, owner of one-seventh of the stock of the Iowa Rolling Mill Company, a corporation under the laws of Iowa, organized for the purpose of rolling and making iron at its works in Burlington, Iowa, prosecutes this action in equity to set aside a sale and conveyance of the works of said corporation to the defendant J. F. Holcomb in pursuance of certain resolutions adopted by the stockholders. A decree was entered dismissing the plaintiff's petition, from which decree he appeals.—*Affirmed.*

GIVEN, J.—* * * It is unquestionably true that a private corporation holds its property as a trust fund for the stockholders, and that, when a majority of the stockholders act together, they are in a sense the corporation, and must act with due regard to the right

²¹ See *Pender v. Lushington* (1877) L. R. 6 Ch. Div. 70 *Burland v. Earle* (1901), L. R. (1902) A. C. 83, especially Lord Davey's opinion at p. 93; *Ervin v. Oregon R. & Nav. Co.* (1886) 27 Fed. 625, 630-2, 23 Blatchf. 517.

In *Bias v. Atkinson* (1908) 64 W. Va. 486, 63 S. E. 395, *held*, the owner of sixty per cent. of the stock stands in a "fiduciary" relation to the corporation and its shareholders. And see, *Young v. Columbia Land & Investment Co.* (1909) 53 Ore. 438, 99 Pac. 936, 101 Pac. 212; *Wolf v. Pennsylvania R. Co.* (1900) 195 Pa. St. 91, 45 Atl. 936 (judgment of majority not lightly to be set aside and fraud must clearly appear).—Eds.

²² Only portion of the opinion is given.—Eds.

of the minority. If the majority decide arbitrarily, and without just cause, to sell the property of the corporation to the prejudice of the minority, and thereby compel the winding up of the business of the corporation, it is a fraud upon the minority, and courts of equity will interfere. If, however, just cause exists for selling the property, as when the corporation is insolvent, and the sale is necessary to pay debts, or where, from any cause, the business is a failure and an unprofitable one, and the best interests of all require it, the majority have clearly power to order the sale, and in such case their acts are not ultra vires. Cook on Stockholders & Corporation Law, sections 656, 662, 667. In this last section it is said: "If, however, the corporation is an unprofitable and failing enterprise, then a sale of all the corporate property with a view to dissolution may be made by the majority of stockholders." It would be a harsh rule that would permit one stockholder to hold the others to their investment when just cause existed for closing the business of the corporation. Lauman v. Lebanon Valley R'y. Co., 30 Pa. St. 42. In Sawyer v. Dubuque Printing Co., 77 Iowa 242, this court recognized the right of the majority of stockholders to make sale of all the corporate property when just cause existed for so doing, and held, under the facts of that case, that the sale was warranted, and was not a fraud upon the minority. The appellant cites at length from Ervin v. Oregon R'y. & Navigation Co., 27 Fed. Rep. 625. In that case there was no claim of necessity for the disposition of the corporate property that was made. It is said: "Plainly the defendants have assumed to exercise a power belonging to the majority in order to secure personal profit for themselves, without regard to the interests of the minority. They repudiate the suggestion of fraud, and plant themselves upon their right as a majority to control the corporate interest according to their discretion." It was plainly held that a court of equity would not tolerate a discretion that did not consult the interest of a minority. The right of a majority to wind up the affairs of a corporation like this, and dispose of its assets, even against the objections of a minority, when the business could no longer be advantageously carried on, is recognized. See Hayden v. Official Hotel Red-Book and Directory Co., 42 Fed. Rep. 875, a case similar in many of its facts to this, and in which the rule just announced was recognized.

We must look to the facts, and see if the action of the majority in ordering the sale in question was warranted by the circumstances. The enterprise was a new one in Iowa. The works had been operated at a loss from the beginning. They had been idle for about one year. The corporation, though solvent, was without the necessary working capital, and unable to secure it. No tangible plan for operating the works was suggested, though the subject was frequently discussed. True, after the adoption of the first resolution to sell, it was proposed to lease to Mr. Roberts, but, as already stated, his offer was indefinite, if it may be called an offer, and

afforded no reasonable ground for expecting that the works could thereby be put in operation. We are inclined to think that this plan was presented by the minority for the purpose of preventing the sale ordered, rather than from any hope of starting the works under it. A marked disagreement had sprung up between the plaintiff and the defendant, Holcomb, neither being willing for the corporation to assume business with the other in even partial control. The Burlington stockholders mainly took sides with the plaintiff, and the Youngstown stockholders with Holcomb. It was apparent that no agreement could be reached by which the works could be operated or leased. No alternative was apparent but to leave the works to rust and decay in idleness, or to sell them. We think the circumstances fully justified the action of the majority in authorizing a sale of the works.

* * * * *

The appellant cites cases announcing the familiar rule that a party holding a fiduciary relation to trust property cannot become a purchaser thereof, either directly or indirectly. It is contended that the defendant Holcomb, in voting the majority of the stock, as already stated, stood in the place of the corporation, and was charged with its trust relation toward the stockholders, and, therefore, within the rule forbidding him from purchasing the property. Mr. Holcomb's relation as a stockholder was not that of agent or trustee, but a joint owner. An agent or trustee is charged with the interests of his principal or cestui que trust, and cannot have any interest adverse thereto. Not so, however, as to a stockholder. He has his own interests to protect, and is not charged with the care of the interests of the other stockholders. They act for themselves. The rule applicable to stockholders is well stated in Rice's Appeal, 79 Pa. St. 204, as follows: "Where a person has the actual control of a corporation, whether such control arises from the ownership of a majority of the shares, or from his position or influence, he is held to most rigid good faith. The onus is upon him to show the fairness of the transaction if it is called in question." This brings us to inquire whether the appellee Holcomb acted in good faith. It is unnecessary that we extend this opinion by here discussing the evidence on this point. It is sufficient to say that purchasers for such property were not numerous, the sale was advertised and open, it was postponed in hope of securing bidders, the minimum price was fixed, and at an open sale the appellee Holcomb made his bid. It is true that the price bid was much less than the cost of the property, but it was all it would bring at an open sale, and, in view of the past failures of this new enterprise, may be said to be equal to the then value of the property. We find no evidence of fraud or bad faith in the transaction. What was done was authorized by

the circumstances, and was done in good faith, and for the best interests of all concerned.

The judgment of the district court is *affirmed*.²³

CHICAGO HANSOM CAB CO. v. YERKES.

1892. 141 Ill. 320, 30 N. E. 667.²⁴

APPEAL from the Circuit Court of Cook County; the HON. LORIN C. COLLINS, Judge, presiding.

Charles T. Yerkes, a stockholder of the Chicago Hansom Cab Co., filed his bill in chancery in the Cook circuit court against that company, Warren Springer, Rose Abernethy, and others, to have a sale and conveyance of real estate and personal property of the company to said Rose Abernethy declared void, and set aside, and for an injunction and the appointment of a receiver. A temporary injunction was issued and a receiver appointed, as prayed. Upon final hearing, Yerkes filed, by consent of court, a supplemental bill to wind up the corporation and sell the real estate, apply the proceeds to the payment of the corporate debts, and distribute any surplus there might be, after such payment, among the stockholders. The court decreed as prayed in the original and supplemental bills, and Springer and Abernethy appeal from that decree.

The Chicago Hansom Cab Co. was organized in 1884 under the general law, as a corporation, for the transportation of persons and property by hansom cabs and carried on this business until 1889. The business proved unprofitable and the company became largely indebted. All of the stockholders were in favor of closing up the affairs of the corporation. A meeting of the stockholders was called, at the instance of Yerkes, for April 13, 1889, to consider the feasibility of selling off the property and closing out the business of the company. At that meeting Yerkes was instructed, by resolution, to consult with an attorney as to the proper and legal way to close the business of the company, and to report to an adjourned meeting on April 15, 1889.

Meanwhile Charles A. Needham, a director in, and the secretary of the Cab Company, had commenced negotiations with Warren Springer, which resulted in their entering into an agreement in writing before the adjourned stockholders' meeting on April 15th, whereby they contracted to purchase, if possible, the stock of the

²³ See also *Shaw v. Davis* (1894) 78 Md. 308, 28 Atl. 619, 23 L. R. A. 294 (minority shareholder's bill dismissed in absence of proof of fraud or illegality on part of majority); *Gamble v. Queens County Water Co.* (1890) 123 N. Y. 91, 25 N. E. 201, 9 L. R. A. 527; *North American Land & Timber Co. v. Watkins* (1901) 109 Fed. 101, 48 C. C. A. 254.—Eds.

²⁴ Statement abridged.—Eds.

Cab Co., and thus obtain control of its property, real and personal, and then to pay the debts of, and wind up the affairs of, the company, and divide its property. Springer's part was to furnish the sum of \$60,000 to purchase the stock and pay the debts of the company.

At the time the stockholders' meeting was held, on the 15th of April, Needham had bought up all the certificates of shares of stock outstanding except those in the names of Yerkes and Pullman, having paid Springer's money therefor, and Pullman had at that time given Springer an option for the purchase of his stock.

At the adjourned meeting of the stockholders, Yerkes made a report to those present, and obtained the opinion of counsel, to the effect, in substance, that while the corporation might sell its property and from the proceeds pay its debts, it was more advisable that it should be closed up by decree of court. Yerkes was then ignorant of the contract that had been made between Springer and Needham, and of the purchases of stock that had been made by Needham for Springer, pursuant thereto. Pullman at that meeting offered to buy the stock of Yerkes at thirty-five cents of its par value, and to pay him \$15,000 at the time. The money was furnished by Springer, and Pullman was acting as his agent in making the offer, though this fact was not known to Yerkes. Yerkes declined the offer, and refused to sell his stock. No action was taken at the meeting in regard to a sale of the property.

At a meeting of the shareholders, held on May 6, 1889, a committee, consisting of the president and secretary, were appointed to sell or mortgage all or part of the property of the company at their discretion, and were authorized to sign, seal, and deliver any mortgage, deed or bill of sale necessary, and to report at an adjourned meeting. The president-treasurer and secretary were Pullman and Needham respectively. Yerkes' 375 shares were voted against the resolution appointing the committee.

The committee reported to a meeting of the shareholders, held on May 8th, that it had sold the business and the entire property of the company and the committee's report was approved and ratified, only the shares of Yerkes being voted in the negative. The sale was made to Springer and Needham, but by direction of Springer the real estate was conveyed to Rose Abernethy, his niece, and the bill of sale of the personal property was also made to her, but both the deed and the bill of sale were delivered to Springer. Those instruments were executed by Pullman, as president, and Needham, as secretary, of the company, and dated May 6, 1889. After the 8th of May, 1889, Needham ran the business that had formerly been carried on by the Chicago Hansom Cab Co., under a lease executed by Rose Abernethy, by Warren Springer, her attorney in fact.

At a special meeting of the board of directors of the company, held on June 8, 1889, they unanimously resolved that the sale made and reported by the president and secretary be ratified and con-

irmed, and that their action and that of the stockholders' meeting be ratified.

SCHOFIELD, J., (after stating the facts.) From the foregoing statement it is clear that when Needham entered into the contract with Springer, the former was a director in the Chicago Hansom Cab Company, and its secretary. As director he owed the duty to the company to preserve its property and protect the company against loss, so far as that could be done by the exercise of ordinary care and diligence, and he could not himself become the purchaser of any property of the corporation which it was his duty to sell. (*Wardell v. Railroad Co.*, 103 U. S. 651.) The contract between Needham and Springer requires the purchase of all the property of the cab company, and the subsequent transfer of the personal property to Needham. It is an entire and indivisible contract, and Needham is therefore directly interested in every part of the claimed contract of sale by the company to Springer.

But it is claimed the authority to make this sale is derived from a vote of a majority of the stockholders. That vote was given at the stockholders' meeting on the 6th of May, 1889, in these words: "Therefore be it resolved, that a committee, consisting of the president and secretary, be appointed to mortgage or sell all or part of the property of the company, at their discretion, and be authorized to sign, seal and deliver any mortgage, deed or bill of sale necessary, and to report at an adjourned meeting, May 8th, at 2:30 P. M., at the same place." This required the exercise of judgment and discretion by both the president and the secretary, and, being a special power, it could not be exercised by one, only; (*Perry on Trusts*, sec. 413; *Hartford Fire Ins. Co. v. Wilcox*, 57 Ill. 180;) and so, necessarily, if one was disqualified to act, neither could act. The resolution of the stockholders invested Needham, as well as Pullman, with a special confidence and trust, which required that he should act solely with a view to the best interests of all the stockholders. But he was disqualified to thus act by reason of his previous contract with Springer, which gave him a personal interest to be promoted by his action under the resolution. The rule is familiar that a trustee is disqualified to act by the intervention of a personal interest in the performance of his duties as trustee. He cannot obtain title to property where he has a duty to perform inconsistent with the character of a purchaser on his own account. *Borders v. Murphy et al.*, 125 Ill. 577.

It is, however, contended, that this sale was ratified by a vote of a majority of the stockholders at their meeting on the 8th of May. Whether, in any case, a ratification is effective, depends upon whether those assuming to ratify might have legally authorized the act to be done in the first instance. At the time this vote was taken, Springer either really owned or had contracted to purchase, and by virtue thereof was entitled to and did control, a majority of the shares of stock,—indeed, all except those owned by Yerkes; and so,

upon the record of the meeting of the 8th of May, the names and votes of Pullman, Himrod, Hagerty, Cotton and Culter, being the votes in favor of the ratification of the sale, are but another form of expressing the name and votes of Springer in favor of it. The question is therefore presented, whether, after it is determined to wind up a corporation and settle its business, it is competent for a holder of a majority of its shares of stock to make or ratify a sale of all its property to himself, against the protest of a holder of a minority of its shares, and in disregard of his rights.

That a holder of a majority of the shares of stock in a corporation may, where the law authorizes a vote of stockholders, so vote, upon any matter of policy in the conduct of the corporation, as to best subserve his own interests, and that this may relate to the ceasing to do corporate business, the winding up of its affairs and the sale of its property, we do not question. But the authorities cited by counsel for appellant (*Gamble v. Queen's County*, 123 N. Y. 91, and *Transportation Co. v. Beatty*, L. R. 12 App. Cas. 589) concede that even in such cases the action resulting from such vote must not be so detrimental to the corporation itself as to lead to the necessary inference that the interests of the majority of the shareholders lie wholly outside of and in opposition to the interests of the corporation and of the minority of the shareholders, and that their action is a wanton or a fraudulent destruction of the rights of such minority. In the cases cited, and, so far as we are informed, in all other cases where the majority of the stockholders may by their votes lawfully affect the interests of the minority of the stockholders, the interests of the minority are, theoretically at least, protected either by directors or trustees of the corporation, who it will not be presumed will betray their trust by acting in the interest of one stockholder to the prejudice of another, or by reason of the transaction being such as is presumed to be alike beneficial to all stockholders,—as, where the corporate property is in good faith appropriated to the payment of the corporate debts, or is sold at a fair sale; and no case cited or within our knowledge goes to the extent of holding that a majority of the stockholders may take the property of the corporation and retain it, if the minority shall elect to deny its right to acquire title to it in that way. Undoubtedly, if in such case the minority of the stockholders shall elect to treat the majority as purchasers, they may do so, and require them to account for the value of the property. Here, Springer, who through Pullman, Himrod, Hagerty, Cotton and Culter, assumes to ratify this sale, is the same Springer who with Needham is the purchaser of the property,—in other words, he assumes to ratify a sale to himself. But a man cannot be both buyer and seller in the same transaction, and where he assumes to be such, his action simply amounts to a taking of the property, and would be quite as valid without as with the circumlocution of the form of a sale through dummies.

The right of a majority of the stockholders to sell the corporate property can by no reasonable construction be held to involve the right to seize the property to their own use. A sale conducted, as it must be, fairly and openly, cannot, theoretically, operate to the prejudice of one stockholder more than to another. There is in such case no presumptive antagonism between the different stockholders. But where, under pretense of a sale to themselves, the majority seize the property and undertake to invest themselves with title, their interests are wholly hostile, for the gain of the one is the loss of the other.

It is a general rule, administered by courts of equity, that where one person has the power of disposition of the property of another without the consent of that other, he shall not be allowed to become personally interested in it himself,—and this without regard to any question of fairness in the immediate transaction,—for he shall not be allowed to occupy a position where self-interest would tempt a betrayal of duty. This rule is plainly applicable here, and it has been so applied in adjudicated cases. It is said in *Cook on Stockholders*, sec. 656: "It is illegal and fraudulent for the majority of the stockholders to purchase the property of the company at a sale authorized by themselves. Such a purchase by the majority may be set aside in the same way and to the same extent that a purchase of corporate property by a director may be set aside." See, also, 2 *Bigelow, Frauds*, (vol. 2, p. 645,) where it is said, "no act of the majority can purge the fraud" of appropriating the common property to their own benefit by any portion of the corporators; and to like effect is the ruling in *Meeker v. Winthrop Iron Co.*, 17 Fed. Rep. 49; *Ervin v. Oregon Railroad & Navigation Co.*, 20 Fed. 577; and see, also, *Menier v. Hooper's Telegraph Works*, 9 L. R. Ch. App. 350; *Brewer v. Boston Theater*, 104 Mass. 378; *Preston v. Grand Collier Dock Co.*, 11 Sim. 327; *Hodgkinson v. N. L. S. Ins. Co.*, 26 Beav. 473; *Atwood v. Merryweather*, L. R. 5 Eq. 464, note.

The action of the board of directors on the 8th of June, as affecting the validity of the sale, is not, under the pleadings, properly before us for consideration. Counsel for appellant are mistaken in saying, as they do, that appellee in his supplemental bill relies upon it. The allegation of the supplemental bill to which reference is made, is this, only: "Your orator further shows, that a majority of the stockholders of said corporation having resolved to discontinue the business of said corporation, the directors of said corporation, since the filing of said bill, have ratified such action of the majority of the stockholders." There is no reference whatever to the sale of the property. "Such action" means, plainly, the resolution to discontinue the business of the company.

We think it unimportant whether the money furnished by Springer, and used by Needham in purchasing the stock of the corporation and in paying for the property claimed to be purchased from it, was that of Rose Abernethy, as said by Springer, at the time he

began negotiating with Needham, or whether, as the evidence strongly tends to prove, it was in fact that of Springer, for in either view the money was furnished and used, as is shown, in performance of the contract between Needham and Springer, and Rose Abernethy can therefore only take subject to that contract, and she must be affected by whatever has been done by Needham and Springer to acquire title to the property.

It appears from the evidence that the directors of the corporation were in the interest and under the control of Springer, so that a demand upon the corporation to bring suit against him would have been unavailing, and the suit is therefore properly brought by Yerkes. *Chicago v. Cameron*, 120 Ill. 447.

We are unable to perceive any sufficient reason for reversing the decree below. It is therefore affirmed.

*Decree affirmed.*²⁵

GLENGARY ETC. MINING CO. v. BOEHMER.

1900. 28 Colo. 1, 62 Pac. 839.

THE following summary of the findings of facts and conclusions deduced therefrom by the trial court fully present the only questions necessary to consider on this appeal.

The Ibex and Glengary Consolidated Mining Companies are corporations organized under the laws of this state, and own adjoining mining properties. The former procured, by purchase, a majority of the capital stock of the latter. The object of the Ibex Company in securing this stock was, to enable it to select a directory of the Glengary which would be under its control, and which, in fact, it did succeed in accomplishing. Its purpose in so doing was to secure a bond and lease on the property of the Glengary Company. It obtained a contract of this character through the directory of this

²⁵ *Accord*, *Woodroof v. Howes* (1891) 88 Cal. 184, 26 Pac. 111, where the court said: "Nor is the resolution at the stockholders' meeting of any consequence; for since the defendants held a majority of the stock and voted at the meeting, they controlled the meeting, and the resolution was, in effect, but their formal consent to their own fraud. It cannot affect the rights of the stockholders who did not consent." (pp. 199-200). See, to similar effect, *Crichton v. Webb Press Co.* (1904) 113 La. 167, 36 So. 926, 67 L. R. A. 76, 104 Am. St. 500; and note, 9 Columbia Law Rev. 550.

But compare *Beatty v. North-West Transportation Co.* (1887) L. R. 12 App. Cas. 589, where a voidable contract, fair in its terms and within the powers of the company, had been entered into by its directors with one of their number as sole vendor, and the Privy Council held, that such vendor was entitled to exercise his voting power as a shareholder in general meeting to ratify such contract and that his so doing could not be deemed oppressive because of his individually possessing a majority of the votes. And, *accord*, *Burland v. Earle* (1901) L. R. (1902) A. C. 83, at p. 94; *Bjorngaard v. Goodhue County Bank* (1892) 49 Minn. 483, 52 N. W. 48.

Cf. Robertson v. Bucklen (1903) 107 Ill. App. 369.—Eds.

company elected at its instance, the proposition for which, as also its terms and conditions, came from the Ibex Company. To annul this transaction the appellees (stockholders of the Glengary Consolidated Mining Company), as plaintiffs, brought this action in the court below. From a judgment and decree in their favor, the defendants appeal.

MR. JUSTICE GABBERT delivered the opinion of the court.

The title to the property belonging to a corporation is vested in it. This it holds subject to its charter and its by-laws, for the use and benefit of its stockholders, and it therefore falls within the strict definition of a trustee, i. e., "one who holds the legal title for the use and benefit of others." *Miner v. Belle Isle Ice Co.* (Mich.) 53 N. W. 218; *Peabody v. Flint*, 6 Allen 52.

Ordinarily, the majority of the stockholders of a corporation have the right to control its affairs, but this right is limited to the legitimate exercise of the corporate powers. Among these is the management of the affairs of the corporation through its proper representatives and officials, in the interest of all shareholders. *Mecker v. Winthrop Iron Co.*, 17 Fed. 48.

No combination of stockholders of a corporation less than the whole will be permitted to manage or control its affairs in their interest alone. Minority stockholders cannot be deprived of their rights by such a combination under the guise of a policy of the corporation dictated by the majority. So far as the rights of the minority are concerned, the majority, in furtherance of their plan to reap a benefit to themselves through a transaction in which the minority do not participate, become the corporation itself, and assume the trust relation occupied by the corporation toward its stockholders. *Miner v. Belle Isle Ice Co.*, *supra*; *Ervin v. Oregon R. & N. Co.*, 27 Fed. 625; *Pearson v. Concord R. Co.*, 62 N. H. 537.

A trustee cannot deal with the trust estate in a matter where his interests would, or might, conflict with his duty to his cestui que trust. In all cases where, without the full knowledge and assent of the cestui que trust, he has assumed to act in the capacity of vendor and vendee, the cestui que trust may void the transaction at his election. No question of the fairness or unfairness of such a transaction can be considered under the state of facts existing in this case. This proposition is fully discussed in the case of *Morgan et al. v. King*, 27 Colo. 539. Applying these principles to the facts found by the trial court, it is clear that its judgment was correct.

The Ibex Company controlled a majority of the stock of the Glengary Company. It secured such stock for the purpose of controlling the Glengary Company in its interest. By assuming control of the Glengary Company, the Ibex Company placed the former at its mercy when contracting for its property. In arranging the price and terms for this property, the Ibex Company was acting for

itself, and not for the interest of the Glengary Company. Ostensibly, the contract was by the latter, but in fact, it was one which the Glengary Company was compelled to accept at the instance of the Ibex Company. In short, the Ibex Company, although pretending to contract with the Glengary Company, was contracting with itself. Being in control of the affairs of that company for this very purpose, it occupied the relation which that company did to its stockholders, i. e., their trustee. The subject-matter of this contract was property of which it was trustee, and in which the shareholders of the Glengary Company, including the minority, were interested as *cestuis que trust*. In law and in fact, it was both parties to this contract. Such a contract is void at the instance of the plaintiffs without regard to whether the Ibex Company was guilty of any actual fraud in obtaining it or not. The judgment of the district court is affirmed.

*Affirmed.*²⁶

WINDMULLER v. STANDARD DISTILLING CO.

1902. 114 Fed. 491.

IN equity. On rule to show cause against issuance of injunction.

KIRKPATRICK, District Judge.—The complainants are the holders of certain shares of the first and second preferred stock of the Spirits Distributing Company, a corporation organized under the laws of the state of New Jersey, upon which the Standard Distilling & Distributing Company have guaranteed a dividend of 6 per cent. upon the first preferred, and 2 per cent. upon the second preferred, stock, during the existence of the said Spirits Distributing Company. It appears from the record that in 1896 the Spirits Distributing Company had an authorized capital of \$7,350,000, of which there was outstanding, in the early part of 1899, \$1,050,000 of first preferred, 7 per cent. cumulative stock; \$1,575,000 of 6 per cent. non-cumulative second stock; and \$3,675,000 of common stock. Among its sources of revenue was a contract with the American Spirits Manufacturing Company, under the terms of which it received a minimum payment of \$100,000 annually, which was to continue for a period of 45 years, unless sooner terminated by a vote of three-fourths of the stock of the said Distributing Company. It also appears that, even with the receipt of \$100,000 provided to be paid by the Spirits Manufacturing Company, the Distributing Company, from the time of its organization until the early part of 1899, had never been in funds with which to pay in full the dividends upon its first preferred stock, nor any part of the dividends

²⁶ As to duty owed by a stockholder exercising a dominating influence, see *Russell v. Rock Run Fuel Gas. Co.* (1898) 184 Pa. St. 102, 39 Atl. 21.—Eds.

upon its second preferred stock. It was proposed, about December, 1898, by one C. H. Eicks, that the stockholders of the Distributing Company should surrender their right to receive 7 per cent. on their first preferred stock and 6 per cent. on their second preferred stock, and that in lieu thereof they should agree to take 6 per cent. on their first preferred and 2 per cent. on their second preferred stock; and, as an inducement for them so to do, he proposed that the said stockholders should surrender to the Standard Distilling & Distributing Company, which had then but recently been organized with a capital of \$24,000,000, all of their common stock in the Distributing Company, which constituted a majority of the whole. He also said to them that in consideration thereof the Standard Company would guarantee the said dividends on the first and second preferred stock, as aforesaid, to the said stockholders during the existence of said Distributing Company. In order to carry out this plan, it became necessary that the charter of the Distributing Company should be amended, and the same was accordingly done, with the consent of every one of its stockholders, including these complainants.

The agreement between the stockholders of the Distributing Company and the Standard Company was carried into effect. The old stock of the Distributing Company was surrendered to its officers, and new stock issued to the shareholders, upon which was stamped the guaranty of the Standard Company, and the common stock of the Distributing Company, being a majority of the whole, was transferred to the Standard Company. From January, 1899, to the date of the filing of the bill, the Standard Company has paid to the complainants the dividends upon their stock in the Distributing Company, as provided in the agreement. The Standard Company took charge of the business of the Distributing Company by qualifying and electing as directors a majority of the board. During the time of their control the business of the company has been successfully prosecuted, and its earnings have so largely increased that during the fiscal year ending June 30, 1901, it showed a profit of upwards of \$30,000. No complaint is made in the bill of the manner in which the property has been administered.

In June, 1899, the Distilling Company of America was organized, and it became the owner of \$22,742,750, par value, of the \$24,000,000, par value, of the stock of the Standard Company, above referred to. It also became the owner, by purchase, of \$2,592,650, par value, of the first and second preferred stock of the Spirits Distributing Company; so that at the time of the filing of this bill the stock of Spirits Distributing Company was held as follows: By the Distilling Company of America, first and second preferred, \$2,592,650; by the Standard Company (of which the Distilling Company, as has been said, owned nearly all of the stock), \$3,675,000, common stock; leaving outstanding stock of all kinds to the amount

of \$232,350, of which the complainants hold but 1,524 shares, 324 of which is first preferred, and 1,200 second preferred.

At a meeting of the board of directors of the Distributing Company it was resolved that, in the judgment of the directors, it was most advisable and for the benefit of the corporation that it should be dissolved. In accordance with the general corporation act of New Jersey, a meeting of the stockholders was called to vote upon the propriety of adopting such a course. The prayer of the complainants' bill is that the Standard Company may be enjoined from voting upon its \$3,675,000, par value, common stock in favor of said proposition, because it has guaranteed the dividends on the stock of the Distributing Company as aforesaid, and that the Distilling Company be enjoined from voting upon its \$2,592,650, par value, of first and second preferred stock, which it has purchased and owns, because it also owns a majority of the stock of the Standard Company, which is the guarantor thereof. That is to say, however advisable and for the benefit of the corporation it may be that the same should be dissolved yet it cannot be done because two-thirds of the stockholders whose votes are necessary to accomplish such results are disqualified from voting by reason of their interest in the cancellation of a guaranty which the complainants now conceive to be adverse to their interests. To carry the doctrine to its logical conclusion would be to hold that, if the guarantor's company and those who own a majority of the stock in the guarantor's company should also be the owners of all the stock in the guaranteed company except one share, the owner of that one share could prevent the dissolution of the company forever, if its charter were perpetual, or compel its operation at a loss until all its assets were wasted or consumed. Section 51 of the general corporation act of New Jersey provides that any corporation organized under it "may hold the shares of any other corporation of that or any other state," and, while the owner thereof, "may exercise all rights, powers, and privileges of ownership, including the right to vote thereon." In respect to the voting power, the rights of a corporation are identical with the rights of an individual, and only those reasons would operate to prevent a corporation from voting on its stock which would effect the same object if the stock was held by an individual.

I have not been referred to any authority which holds that one stockholder is in any sense a trustee for other stockholders, or that he is debarred from voting on his stock according to what he may conceive to be his interest, or in a way which may result in a benefit to himself, and which other stockholders may not enjoy. Directors, by whomsoever elected, are the representatives of all the stockholders, and, as such, are charged with the duty of administering the affairs of the company for the equal benefit of their cestuis que trustent. But the doctrine is new that the stockholders are trustees one for another, or that an interest of one stockholder, which in the judgment of another stockholder may seem to be ad-

verse to his own, can operate to prevent him from voting on his own stock as he sees fit.

In the case of *Transportation Co. v. Beatty*, 12 App. Cas. 589, one of the directors owned a majority of the stock of the corporation, and at a meeting of the shareholders, by reason of his majority, he caused to be passed a resolution ratifying a contract to sell to the company upon advantageous terms, a vessel belonging to himself. In passing upon the propriety of his right to vote, the court said:

"Unless some provision to the contrary is to be found in the charter or other instrument by which the company is incorporated, the resolution of a majority of the shareholders, duly convened, upon any question with which the company is legally competent to deal, is binding upon the minority, and consequently upon the company; and every shareholder has a perfect right to vote upon any such question, although he may have a personal interest in the subject-matter opposed to or different from the general or particular interests of the company. A shareholder has a perfect right to exercise his voting power in such manner as to secure the election of directors whose views on policy agree with his own, and to support those views at any shareholders' meeting."

The court cannot be called upon to manage the internal affairs of corporations, or to determine whether this or that stockholder is disqualified from voting upon one or another question which may be presented to stockholders for their consideration by reason of his own interest. If the directors, who are the trustees of all, conspire with a few or some of the stockholders to deprive the others of their property, the court will interfere to see that justice is done. The court will not permit the directors to divert the business of the corporation so that a sale and sacrifice of its assets will become obligatory, and the distribution of the proceeds unequal among its shareholders. This is the doctrine which is at the foundation of the opinion in the case of *Farmers' Loan & Trust Co. v. New York & N. R. Co.*, 150 N. Y. 410, 44 N. E. 1043, 34 L. R. A. 76, 55 Am. St. Rep. 689, and *Ervin v. Navigation Co.* (C. C.) 27 Fed. 625.

No case has been brought to the attention of the court where any stockholder has been deprived of his right to vote on his stock in such a way as may, in his opinion, best subserve his own interests. He may vote his stock as he pleases for the purpose of his own interest, but he may not sell or cause to be sold, assets and keep the consideration. *Menier v. Telegraph Works*, 9 Ch. App. 350. In *Gamble v. Water Co.* (N. Y.) 25 N. E. 201, a stockholder's right to vote was questioned because of interest, and the court of appeals, reversing the decision of the lower court, said:

"A shareholder has a legal right, at a meeting of shareholders, to vote upon a measure, even though he has a personal interest therein separate from other shareholders. At such a meeting each shareholder represents himself and his own interests, and he in no sense acts as the representative of others. The law of self-interest

has at such time very great and proper sway. There can be little doubt, too, that at such meetings those who do vote on their own stock vote upon it in the light solely of their own interest, or at least in what they conceive to be their own interest."

In the case at bar the court is not in possession of facts which would enable them to determine whether the interests of the corporation, as distinct from the interests of the individual shareholders, require that it should be dissolved. Under the general corporation act of the state of New Jersey, any corporation may be dissolved whenever in the judgment of the board of directors it shall be deemed advisable and most for the benefit of such corporation that it should be dissolved; provided that, at a meeting of the stockholders called for the purpose of passing upon the propriety of such dissolution, two-thirds in interest of all the stockholders shall consent thereto. Laws 1896, c. 185. There is no provision in the law which authorizes the court to review the judgment of the directors as to the advisability of dissolution. And in 4 Thomp. Corp. § 433, it is said:

"It is believed that no case can be found in which a court of equity has granted an injunction at the suit of a minority stockholder against the majority to prevent them from discontinuing the business of the corporation and winding up its affairs."

It is urged in behalf of the complainants that it would be inequitable to allow the Standard Company, after having received a valuable consideration for their guaranty, by their own act to dissolve the corporation, and thereby cancel its said obligation. But it must be remembered that, in the proposition made to the stockholders of the Distributing Company by Mr. Eicks, Mr. Eicks said that, if such stockholders would consent to a reduction of the rate of their dividends, he would procure the Standard Company to guarantee and pay, during the existence of the company, dividends at the rate of 6 per cent. per annum on the first preferred, and 2 per cent. per annum on the second preferred, stock of the Distributing Company. To that proposition the complainants assented, and they did so with the knowledge that at any time, under the laws of the state of New Jersey, two-thirds in interest of the shareholders of the Distributing Company could dissolve the company, and thereby put it out of existence. They are in no position to complain if, in accordance with the terms of the agreement, the Standard Company and the Distilling Company, who are the stockholders of the Distributing Company, propose to put an end to their liability thereunder.

Other reasons are urged in behalf of the defendant company why this injunction should not be granted, but, having come to the conclusion that the Standard Company and the Distilling Company of America are not prohibited from exercising their right to vote at the stockholders' meeting upon the question of dissolution sub-

mitted by the board of directors, it is not necessary to enter into any discussion of them.

*For the reasons already stated, therefore, the rule to show cause in this case must be discharged.*²⁷

WHEELER v. ABILENE NAT. BANK BLDG. CO.

1908. 159 Fed. 391.

APPEAL from the Circuit Court of the United States for the District of Kansas.

Before SANBORN, HOOK, and ADAMS, Circuit Judges.

SANBORN, Circuit Judge.—Two holders of the minority of the stock of the Abilene National Bank Building Company, a corporation, brought a suit in the court below to avoid a sale of all the property of the corporation to Hiland Southworth, who was the president of the corporation, its creditor, one of its board of directors, and the holder of the majority of its stock. After the issues had been joined the case was referred to a master to find the facts. He found them; exceptions to his finding were filed and overruled, and the court dismissed the bill. A portion of the testimony taken before the master appears to be printed in the transcript of the record before us, but no order of the court below that the master should return into court the evidence he obtained, and no certificate of the master that he has done so, or that the record contains that evidence, or a correct transcript of it, can be found. For this reason, and because the facts essential to a determination of the case appear on the face of the master's finding, the exceptions to his report and the evidence printed will not be further noticed. * * *

The following facts appear from the pleadings and the findings of the master: The only property of the corporation was a lot and building in Abilene, which was sold to Southworth, the holder of the majority of the stock of the company, in June, 1904. The fair value of this property was \$2,500. The corporation had power to buy, sell, and deal in real estate, and it had issued 173 shares of stock. The complainants, who lived in the state of Vermont, owned 46 shares. The defendant Southworth, who resided in Abilene, in the state of Kansas, owned 101 shares. The defendants Humphrey, Malott, Ella M. Southworth, the wife of Southworth, and Stella Duckworth, his stenographer, held 1 share each which Southworth had transferred to them to qualify them to act as directors. Southworth was the president. Stella Duckworth was secretary. South-

²⁷ *Accord*, Windmuller v. Standard etc. Distributing Co. (1902) 115 Fed. 748. See Rothchild v. Memphis etc. R. Co. (1902) 113 Fed. 476; and note, 22 Harv. Law Rev. 591-3.—Eds.

worth, Mrs. Southworth, Stella Duckworth, Humphrey and Malott constituted the board of directors. The corporation owed Southworth, but its property was of greater value than the amount of its debts. Malott and Humphrey inquired and found that \$2,500 was a fair price for the property, and the board sold and the corporation conveyed it to Southworth for that amount, paid the debts of the corporation, declared a dividend on its stock, and remitted the proper amount to each stockholder; but the complainants refused to accept their dividends. In July, 1904, Wheeler, one of the complainants, objected to this sale and told Southworth he would give \$3,500 for the property. In August, 1904, Southworth and wife conveyed the lot and building to the corporation. On August 29, 1904, Wheeler sent a letter to Stella Duckworth, the secretary of the corporation, which she received, wherein he wrote that if the property was offered for sale he desired an opportunity to bid upon it; but this letter was never brought to the attention of any meeting of the stockholders or of any meeting of the directors. On November 10, 1904, the board of directors accepted the reconveyance of the property. Malott said he had made diligent inquiry regarding its value, and that he could find no one who would place a higher value than \$2,500 upon it. Southworth offered \$2,500; the board unanimously voted to sell it to him for that price, and the corporation again conveyed it to him. Legal notice that there would be an annual meeting of the stockholders on December 6, 1904, to elect a board of directors and to transact such other business as might come before the meeting, was given. There were present at the meeting Hurd, Humphrey, Malott, Stella Duckworth and Southworth, who together represented 111 shares of stock, and they voted unanimously to confirm the sale to Southworth for \$2,500. Southworth and the other directors acted in good faith. Upon these facts the court below dismissed the bill, and the complainants appealed.

The question which this case presents is: May the holder of the majority of the stock of a corporation make a sale to himself, unassailable in equity, of all the property of the corporation for its fair value, when he knows that the value is only five-sevenths of the amount which the corporation can obtain for it. It is not material to the determination of this issue whether the notice of the stockholders' meeting specified, or failed to state, that the question of the confirmation of the sale to Southworth would be there considered, or whether or not the other proceedings of the defendants complied with the requirements of the law; and for the purpose of this decision it will be conceded, but it is not decided, that all the proceedings of the parties and of the corporation were in strict accordance with the forms of law. The objection to this sale lies deeper. It is that it was violative of the duty of a fiduciary.

A corporation holds its property in trust for its stockholders. The stockholders have a joint interest in the same property and in

the same title. Community of interest in a common property or title imposes a community of duty and a mutual obligation to do nothing to impair either. It creates such a fiducial relation as makes it inequitable for any of those who thus share in the common property to do anything to or with it for their own profit, to the detriment of others who have the same rights. *Jackson v. Ludeling*, 21 Wall. (U. S.) 616, 622, 22 L. ed. 492; *Jones v. Missouri Edison Electric Co.*, 144 Fed. 765, 771; 75 C. C. A. 631, 637; *Booker v. Crocker*, 132 Fed. 7, 8, 65 C. C. A. 627, 628.

The holder of the majority of the stock of a corporation has the power, by the election of biddable directors and by the vote of his stock, to do everything that the corporation can do. His power to control and direct the action of the corporation places him in its shoes, and constitutes him the actual, if not the technical, trustee for the holders of the minority of the stock. He draws to himself and uses all the powers of the corporation. In effect he holds an irrevocable power of attorney from the minority stockholders to manage and to sell the property of the corporation, for himself and for them. Times, places, and notices of meetings of the directors and of meetings of stockholders become of secondary importance, because the presence, the vote and the protest of holders of the minority of the stock are unavailing against the will of the holder of the majority. They can act and contract regarding the corporate property, they can preserve and protect their interests in it, only through him and through the courts.

This devolution of unlimited power imposes on a single holder of the majority of the stock a correlative duty, the duty of a fiduciary or agent, to the holders of the minority of the stock, who can act only through him, the duty to exercise good faith, care and diligence to make the property of the corporation produce the largest possible amount, to protect the interests of the holders of the minority of the stock, and to secure and pay over to them their just proportion of the income and of the proceeds of the corporate property. (Any sale of the property of the corporation by him to himself for less than he could obtain for it from another or any other act in his interest to the detriment of the holders of the minority of the stock, becomes a breach of duty and of trust, renders the sale or act voidable at the election of the minority stockholders, and invokes plenary relief from a court of chancery.) *Jackson v. Ludeling*, 21 Wall. (U. S.) 616, 622, 22 L. ed. 492; *Jones v. Missouri Edison Electric Co.*, 144 Fed. 765, 771, 75 C. C. A. 631, 637; *Burnes v. Burnes*, 137 Fed. 781, 790; 70 C. C. A. 357, 366; *McCourt v. Singers-Bigger*, 145 Fed. 103, 107, 76 C. C. A. 73, 77; *Pepper v. Addicks* (C. C.) 153 Fed. 383, 405; *Wardell v. Railroad Company*, 103 U. S. 651, 658, 26 L. ed. 509; *Menier v. Hooper's Telegraph Works*, 9 Ch. App. Cas. 350, 352, 353; *Goodin v. Cincinnati & Whitewater Canal Co.*, 18 Ohio St. 169, 182, 183, 98 Am. Dec. 95; *Ervin v. Oregon Ry. & Nav. Co.* (C. C.) 20 Fed. 577, 580, Id., 27 Fed. 625, 632; 2 Story's Eq. Jur.

§§1261, 1262; *Sage v. Culver*, 147 N. Y. 241, 247, 41 N. E. 513; *Farmers' Loan & Trust Co. v. N. Y.*, etc., R. R. Co., 150 N. Y. 410, 425, 430, 44 N. E. 1043, 34 L. R. A. 76, 55 Am. St. 689; *Hinds v. Fishkill*, etc., Gas Co. (Sup.) 88 N. Y. S. 954, 957; *Meeker v. Winthrop Iron Co. (C. C.)* 17 Fed. 48; *Sidell v. Missouri Pac. R. Co.*, 78 Fed. 724, 727, 24 C. C. A. 216, 219; *Barr v. N. Y.*, L. E. & W. R. R. Co., 96 N. Y. 444, 449, 451, 456; *Wright v. Oroville M. Co.*, 40 Cal. 20, 27; *Pondir v. N. Y.*, L. E. & W. R. R. Co., 72 Hun (N. Y.) 384, 390, 25 N. Y. S. 560; *Gregory v. Patchett*, 33 Beavan 595, 607; *Meyer v. Staten Island Ry. Co.*, 7 N. Y. St. 245, 248. The reason for this rule is the detriment to the holders of the minority of the stock from such sales and transactions, and not the benefit the holder of the majority derived therefrom. *Symmes v. Union Trust Co. (C. C.)* 60 Fed. 830, 865; *Memphis & Charleston R. R. Co. v. Woods*, 88 Ala. 641, 7 So. 108, 7 L. R. A. 605, 16 Am. St. 81. It is the duty of the master of the corporation who sells its property to procure the highest possible price for it (*Jackson v. Ludeling*, 21 Wall. (U. S.) 616, 625, 22 L. ed. 492); and, if he sells it to himself for less, the sale is voidable by the holders of the minority of the stock at their option, although he paid the fair market value for it. *Miller v. Brown*, 1 Nebr. (Unof.) 754, 95 N. W. 797.

The principles which have been briefly reviewed and the decisions which have been cited in support of them spring from the law's jealous care of the fiduciary relations, from its persistent endeavor to prevent a conflict of duty and interest by removing from every person in such a relation every possible temptation to advance his own welfare in disregard of his duty to his correlate, by avoiding every transaction in which he has endeavored to do so. They have been repeatedly discussed and affirmed in the Supreme Court and in this court, and a more extended consideration of them is now unnecessary. Suffice it to say that one of the familiar rules they sustain and illustrate is that one may not be an agent to sell for another and a purchaser at the same time, that such a sale is voidable at the election of the principal, and that under this rule, and under the equitable principles to which reference has been made, the sale of Southworth cannot be sustained in a court of chancery. He grasped and held all of the powers of the corporation. It could act and contract only through him. He was the agent through whom, and through whom alone, under the law, the corporation and the holders of the minority of its stock could sell its property. He sold it to himself by his use of the powers of the company. If that sale had been fair and open, after full opportunity to all interested to bid, for the highest amount that could be obtained for the property, it might have been sustained. But it was made for \$2,500 to the holder of the majority of the stock, who was one of the members of the board of directors and the president of the company, and to whom one of its stockholders had offered \$3,500 for the property

only about four months before the sale, and who had written the secretary that, if it was offered for sale, he desired to bid.

The president of the corporation and the members of the board of directors may have acted in good faith, in the sense that they had no intent to inflict injury upon the holders of the minority of the stock. They may have believed that if they procured for the corporation the fair value of the property they discharged their whole duty. In this they were in error. If they could have obtained for the property by an open and honest sale \$1,000 more than it was worth, it was their duty to the stockholders of the corporation to do so, and the holder of the majority of the stock could not be permitted to sell it to himself for less.

The sale, however, is voidable, not void, and the court below may require a complainant who seeks equity to do equity. The decree below is accordingly reversed, and the case is remanded to the Circuit Court, with directions to enter an interlocutory decree to the effect that the sale to Southworth be avoided, and the property be sold by a master, on condition that, within 60 days after the entry of the interlocutory decree, the complainants, or one of them, offers to pay for the property and deposits with the clerk of the court \$3,000, to be applied in payment for the property at the master's sale in case no one offers more, and in case the depositor proves to be the highest bidder, otherwise to be returned to him, and in case such a deposit is made to enter a decree for the sale of the property by a master, for a proper accounting, and for such other relief as may be proper, and in case no such deposit is made to enter a decree of dismissal of the bill for failure to comply with the conditions specified; and it is so ordered.²⁸

✓

Section 9.—Transfer of Stock.

BARRETT v. KING.

1902. 181 Mass. 476, 63 N. E. 934.

TORT for the alleged conversion of twenty shares of the capital of the Continental Brewing Company against Charles A. King and that corporation. Writ dated July 3, 1899.

²⁸ *Ervin v. Oregon R. & Nav. Co.* (1886) 27 Fed. 625, 23 Blatchf. 517; *Central Trust Co. v. Bridges* (1893) 57 Fed. 753, 6 C. C. A. 539, *semble* (construction contract made by a dominating stockholder with a railroad company, *per* Taft, J.); *Mumford v. Ecuador Development Co.* (1901) 111 Fed. 639; *Geddes v. Anaconda Copper Mining Co.* (1912) 197 Fed. 860, *Accord*.

See also, *Crichton v. Webb Press Co.* (1904) 113 La. 167, 36 So. 926, 67 L. R. A. 76, 104 Am. St. 500; *Farmers' Loan & Trust Co. v. N. Y. & N. R. Co.* (1896) 150 N. Y. 410, 44 N. E. 1043, 34 L. R. A. 76, 55 Am. St. 689; *Continental Ins. Co. v. N. Y. & H. R. Co.* (1907) 103 App. Div. (N. Y.) 282, 93 N. Y. S. 27 (affd. 187 N. Y. 225, 79 N. E. 1026.) And see note, 9 Columbia Law Rev. 357.—Eds.

In the Superior Court HOPKINS, J., ordered a verdict for the defendants; and the plaintiff alleged exceptions.

The face of the certificate for the shares in question contained the following: "This certifies that William A. Holmes, of Boston, Mass., is the owner of twenty (20) shares of the capital stock of the Continental Brewing Company, and said shares are transferable only in person, or by attorney duly constituted, on the books of the Company on the surrender of this certificate, duly executed, and are only transferable in accordance with the By-Laws of the company which are hereon endorsed, and with such other By-Laws, rules and regulations as the stockholders shall for such purpose ordain and publish."

On the back of the certificate were the following extracts from by-laws:

"Section 2. No transfer of any stock of this Corporation shall be of any effect as concerns the Corporation until the certificate therefor has been duly executed and surrendered for cancellation, and the transfer has been registered upon the books of the Company."

"Section 4. No stockholder shall sell or otherwise dispose of the whole or any part of his stock unless he shall, at least thirty days previous thereto, have offered in writing to sell the same to the Board of Directors upon the same terms and for the same price as he shall have been offered by his prospective purchaser, and such offer to said directors shall not have been accepted within that period.

"In case any stock so offered under this provision of this By-Law is accepted by the Board of Directors, said Board may sell said stock, either in whole or in part, for a price not less than the market value of said stock, to any stockholder, or to any person engaged in the business of bottling or of vending beer or ale or other malt beverage, or dealing in malt or malt extracts. If said offer to said directors shall not have been accepted within said period of thirty days, no sale by said stockholder at a less price than the price mentioned in his said offer to the directors shall be valid, and no transfer shall in such case be made by the Company."

HOLMES, C. J.—This is an action of tort for the conversion of twenty shares of stock in the Continental Brewing Company, by a refusal to transfer it to the plaintiff on the books of the company. It may be assumed for the purposes of decision that the stock was purchased on the plaintiff's behalf, but it stood in the name of one W. A. Holmes, who indorsed the certificate and handed it over to the plaintiff as soon as he got it. This certificate was expressed to be transferable only in accordance with the by-laws of the company printed upon it, and one of those by-laws forbade a disposition of the stock unless the stockholders, at least thirty days previous thereto, should have offered in writing to sell the same to the board of directors upon the same terms and the offer had not been accepted.

There was no evidence that Holmes had made such an offer and the judge of the Superior Court ordered a verdict for the defendant, subject to the plaintiff's exception. If this course was right it is unnecessary to consider the various minor questions that were raised while the plaintiff's case was going in.

It is argued that the plaintiff is not within the by-law because she was an undisclosed principal and should be regarded as having had the legal title from the moment of the purchase with her money. But we might as well talk about an undisclosed principal in a deed of land. The corporation has nothing to do with undisclosed equities or undisclosed relations. The only person whom it can recognize as owner is the one who appears as such on its books. *J. Wentworth Co. v. French*, 176 Mass. 442. And if, after it has issued a certificate, some one else claims rights in the stock, it is entitled to require that person, before disturbing it, to establish his right in accordance with the lawful conditions which the certificate expresses. We may observe that in the plaintiff's argument she is called an original subscriber, but this would be inaccurate even if the argument were better than it seems to us. Holmes purchased of the defendant King. We do not perceive, however, that this fact is material on either side.

But it is said that if the plaintiff has to claim by virtue of Holmes's indorsement, then she has a legal title to the stock by transfer. For it is said that the by-laws do not purport to make invalid a transfer without a previous offer to the directors, and that if they do they are against public policy and void. As to the meaning of the by-laws we shall not spend argument. They certainly did not mean to leave the company and the directors liable to an action for refusing to carry out what they prohibit. As to public policy, we see nothing in the provision contrary to that, at least as between the plaintiff and the corporation. The law of West Virginia, under which the defendant corporation was organized, is not before us. Under the law of Massachusetts, the stipulations, considered as a contract between the corporation and Holmes, undoubtedly would be lawful. *New England Trust Co. v. Abbott*, 162 Mass. 148. And this decision goes far to sustain the by-law as such, by consequence. See *Feckheimer v. National Exchange Bank of Norfolk*, 79 Va. 80, 83. Furthermore, looking at the stock merely as property, it might be said that, so far as appears and probably in fact, it was called into existence with this restriction inherent in it, by the consent of all concerned. See *Braintree Water Supply Co. v. Braintree*, 146 Mass. 482, 488. This is not the case of a by-law attempting to cut down the rights of property already acquired, against the will of some of the owners. The whole stock originally was issued to the defendant King in payment for the plant and he was desirous of keeping it in the hands of consumers, that is of liquor dealers. And this suggests a further consideration. Stock in a corporation is not merely property. It also creates a personal relation analogous otherwise than tech-

nically to a partnership. Notwithstanding decisions under statutes, like *In re Klaus*, 67 Wis. 401, there seems to be no greater objection to retaining the right of choosing one's associates in a corporation than in a firm. In *Price v. Minot*, 107 Mass. 49, 60, no doubt was thrown on the validity of a by-law much more questionable than this.

We perceive no difficulty in the case except the somewhat academic question whether the by-law accepted by Holmes when he accepted the certificate operates only by way of contract and should be pleaded as such, or whether it affects the character of the property itself as we have suggested. In our opinion it at least so far affects the character of the act relied upon as a conversion as to prevent its being a wrong. Therefore it is unnecessary to analyze the matter more nicely or to inquire whether, apart from the by-law and more general difficulties, (*Lowell, Transfer of Stock*, §§ 11, 238), the plaintiff had such a legal title as to warrant an action of trover. It is settled that an assignee of a certificate of stock has a standing in a court of law to maintain assumpsit, (*Sargent v. Franklin Ins. Co.*, 8 Pick. 90; *Sargent v. Essex Marine Railway*, 9 Pick. 201), or an action on the case, (*Hussey v. Manufacturers' & Mechanics' Bank*, 10 Pick. 415); and in *Bond v. Mount Iron Co.*, 99 Mass. 505, an action was maintained counting in trover and assumpsit but without consideration as to which was the proper form. As against the corporation the plaintiff would not be the legal owner even if she had a present right to become so. This action is for a conversion of the stock, not of the certificate. If trover can be extended to such a case, it would seem open to question whether any one but the legal owner could be regarded as having the necessary present right of possession. But this suggestion need not trouble us here.

*Exceptions overruled.*¹

¹ In *Borland's Trustee v. Steel Bros. & Co., Lim.* (1900), L. R. (1901) 1 Ch. Div. 279, held that provisions in a corporation's articles compelling a stockholder desiring to sell his shares at any time during the duration of the corporation to sell them to particular persons at a designated price were valid and not repugnant to absolute ownership. See also, *Moffatt v. Farquhar* (1878) L. R. 7 Ch. Div. 591. But see *Bloede Co. v. Bloede* (1896) 84 Md. 129, 34 Atl. 1127, 33 L. R. A. 107, 57 Am. St. 373. Cf. *Sargent v. Franklin Ins. Co.* (1829) 8 Pick. (Mass.) 90, 19 Am. Dec. 306 (by-law limiting transfer to assignment at the corporate office personally or by attorney with the president's assent is void.)

Transferee is entitled to transfer on the books, although the corporation may think the transfer is prejudicial to its interests. That inquiry into motive, in general, is immaterial, see *Rice v. Rockefeller* (1892) 134 N. Y. 174, 31 N. E. 907, 17 L. R. A. 237, 30 Am. St. 658. Cf. *Senn v. Union Premium Mercantile Co.* (1905) 115 Mo. App. 685, 92 S. W. 507 (registration refused where purpose was to wreck corporation); *Gould v. Head* (1890) 41 Fed. 240. In *State ex rel. Townsend v. McIver* (1870) 2 S. Car. 25, *Moses, C. J.* said (p. 43): "It is very true that whatever rules they may have adopted for the transfer of their stock must be observed, but when a compliance with them is offered, the officers are not at liberty to inquire into the motives of the seller and the vendee, the purpose which prompts the sale, or what will be the effect * * *." And so, *State ex rel. Page v. Smith* (1876) 48 Vt. 266, 290.—Eds.

THIRD NAT. BANK v. BUFFALO GERMAN INS. CO.

1904. 193 U. S. 581, 48 L. ed. 801, 24 Sup. Ct. 524.*

THE Third National Bank of Buffalo, spoken of hereafter as the bank, was organized on the ninth of February, 1865, and its articles of association contained the following:

"That the board of directors shall have power to make all by-laws that may be proper and convenient for them to make under said act for the general regulation of the business of the association and the management and administration of its affairs, which by-laws may prohibit, if the directors shall so determine, the transfer of stock owned by any stockholder who may be liable to the association either as principal debtor or otherwise without the consent of the board."

In virtue of the authority assumed to be conferred by the foregoing provision, the board of directors adopted in February, 1865, a by-law as follows:

"Transfers of Stock.—Sec. 15. The stock of this bank shall be assignable only on the books of this bank, subject to the restrictions and provisions of the act, and a transfer book shall be kept in which all assignments and transfers of stock shall be made. No transfers of the stock of this association shall be made without the consent of the board of directors by any stockholder who shall be liable to the association either as principal debtor or otherwise, which liability shall be a lien upon the said stock and all the profits thereof, and dividends and certificates of stock shall contain upon them notice of this provision."

Pursuant to this by-law the stock certificates of the bank were thus framed:

"This is to certify that ——— is the owner of ——— shares of one hundred dollars each of the capital stock of the Third National Bank of Buffalo, subject to the lien or liens referred to in section 15 of the by-laws of said bank, in the following words: 'No transfer of the stock of this association shall be made without the consent of the board of directors, by any stockholder, who shall be liable to the association either as principal debtor or otherwise, which liability shall be a lien upon the said stock and all profits thereof and dividends.' And the said stock is transferable only on the books of the bank by him or his attorney on the surrender and cancellation of this certificate and compliance with the said by-laws."

Emmanuel Levi became the registered holder and owner of 450 shares of the capital stock, evidenced by certificates, in the form just stated. Levi borrowed money from the bank upon his promissory notes, secured by various collaterals. On the first day of October, 1890, he applied for a further loan, which the bank agreed to make, provided the new loan was endorsed by Louis Levi, a son

*Statement abridged. Portion of opinion omitted.—Eds.

of Emmanuel. At that time, in a conversation between the president of the bank and Levi, it was understood that all the stock held by Levi in the bank should be considered as additional security for his entire loan. When this conversation took place, however, the certificates evidencing Levi's stock were in his possession, and no formal pledge or subsequent delivery of the certificates of stock to the bank took place.

A few months after (on December 3, 1890) Emmanuel Levi borrowed \$25,000 from the Buffalo German Insurance Company, hereafter spoken of as the insurance company, and secured this loan by pledging, delivering and assigning to the insurance company his certificates of stock in the bank. The written contract of pledge gave the insurance company power, in default of payment of the loan at its maturity, to sell the stock at public or private sale after notice and apply the proceeds to the debt. On August 13, 1891, and on May 5, 1892, Levi borrowed additional sums from the insurance company and secured these loans by a pledge and assignment of his remaining stock in the bank. These contracts of pledge also contained a power of sale similar to that conferred by the first contract. In June, 1893, Emmanuel Levi died, and Louis and Rosa Levi were appointed and qualified as his executors. On the 9th of June, 1896, there was due to the insurance company on the notes of Levi, secured by the pledge of his stock as above stated, the sum of \$55,000 of principal, with certain unpaid interest. On that date the insurance company served upon the executors of the estate of Levi a demand for the payment of the debt, accompanied with a notice that if payment were not made the stock would be sold and the proceeds applied to the debt. Payment not having been made, after adequate notice, the attorneys for the bank, the attorneys of the executors of Levi, and one of the executors being present, the stock was sold at public auction, and was bought by the insurance company for the sum of \$44,000, that being the highest bid offered. The insurance company thereupon presented to the bank the certificates of stock, the assignment thereof and the evidence of the purchase at auction, and demanded a transfer to its name. This the bank refused on the ground of Levi's indebtedness to it. Subsequently the insurance company filed its bill, praying that the bank be decreed to transfer the stock and pay the dividends which had accrued thereon since the date of the demand to transfer. The bank by its answer set up the debt due by Levi to it, asserting that under the provision of its articles of association and by-laws, as well as under the terms of the certificates of stock and the agreement with Levi, it had the right to apply the dividends on the stock, accrued since the purchase by the insurance company, to its debt, and, indeed, having a prior lien upon the stock for its debt, had the right to withhold the transfer of the stock until the debt due it by Levi or his estate was paid.

* * * * *

MR. JUSTICE WHITE, after making the foregoing statement, delivered the opinion of the court.

It is obvious that the bank had no lien on the stock of Levi as the result of an express contract of pledge. * * *

This brings us to the real question in the case which is, the validity and effect of the provisions of the charter and by-law of the bank forbidding a transfer of stock where the stockholder was indebted to the bank and the insertion of a condition to the same effect in the certificates of stock which were held by Levi, and which he delivered to the insurance company, as collateral, when he borrowed money from that company. If those provisions were valid it is obvious that the insurance company took the stock subject to the paramount right which the bank possessed. If, on the other hand, the condition in question was void because repugnant to the text of the national bank law and in conflict with the public policy which that act embodies, it is equally clear that there was no lien in favor of the bank, and the title of the insurance company, derived from its pledge and purchase, was paramount to any assumed right of the bank to refuse to transfer the stock in order to enforce a lien which, it was asserted, the bank possessed as a result of the condition in question. (That the provisions referred to were void because coming within the last mentioned category will become apparent from a brief consideration of the national bank law found in the Revised Statutes as elucidated by its evolution from the acts of 1863 and 1864, and as expounded by the previous decisions of this court.

National banks were first created by the act of 1863. (12 Stat. 665.) By section 36 of that act it was provided:

"That the capital stock of any association formed under this act shall be divided into shares of one hundred dollars each, and shall be assignable on the books of the association in such manner as its by-laws shall prescribe; but no shareholder in any association under this act shall have power to sell or transfer any share held in his own right so long as he shall be liable, either as principal, debtor, surety or otherwise, to the association for any debt which shall have become due and remained unpaid, nor in any case shall such shareholder be entitled to receive any dividend, interest or profit on such shares so long as such liabilities shall continue, but all such dividends, interests and profits shall be retained by the association and applied to the discharge of such liabilities; and no stock shall be transferred without the consent of a majority of the directors while the holder thereof is thus indebted to the association."

Section 37 of the same act provided that—

"No banking association shall take, as security for any loan or discount, a lien upon any part of its capital stock, . . . and no such banking association shall be the purchaser or holder of any portion of its capital stock or of the capital stock of any other incorporated company, unless such purchase shall be necessary to prevent loss upon a debt previously contracted in good faith on secur-

ity which, at the time, was deemed adequate to insure the payment of such debt, independent of any lien upon such stock; or in case of forfeiture of stock for the non-payment of installments due thereon, and stock so purchased or acquired shall in no case be held by such association so purchasing for a longer period of time than six months, if the same can, within that time, be sold for what the stock costs."

The act of 1863 was expressly repealed (sec. 62) by the act of 1864. (13 Stat. 99.) The repealing act, however, contained the following:

"Provided, that such repeal shall not affect any appointments made, acts done or proceedings had, or the organization, acts or proceedings of any association organized or in the process of organization under the act aforesaid."

The act of 1864, which contained a repealing clause subject to the foregoing proviso, re-enacted in completer form the entire law as to national banks. The subjects which had been embraced by section 36 of the act of 1863 were contained in section 12 of the act of 1864, in part, as follows:

"The capital stock of any association formed under this act shall be divided into shares of one hundred dollars each, and be deemed personal property, and transferable on the books of the association in such manner as may be prescribed in the by-laws or articles of association; . . ."

The remaining provisions of the section related solely to the double liability of the shareholders. It hence follows that all the provisions found in section 36 of the act of 1863, empowering the board of directors of a national bank to withhold a transfer in case of a debt due by a stockholder to a bank, were not only omitted from the new act, but were expressly repealed. The provision found in the thirty-seventh section of the act of 1863, prohibiting an association from making any loan or discount on the security of the shares of its own capital stock, was re-expressed in a substantially identical, though somewhat more amplified, form of statement in section 35 of the new act. The provisions of the act of 1864, in the particulars in question, are now embodied in sections 5139 and 5201 of the Revised Statutes.

When this history of the legislation is considered it becomes apparent that the clause inserted in the articles of association, in the by-laws and the certificates of stock of the bank here being considered was directly repugnant to the act of 1864, and amounted simply to an attempt on the part of the bank to exercise the power which was granted under the act of 1863, but which was denied by the act of 1864. And this result was long since pointed out by the decisions of this court. In *Bank v. Lanier*, 11 Wall. 369, the case was this: The First National Bank of South Bend was organized under the act of 1863. A by-law of the bank provided that "the stock of the bank should be assignable only on its books, subject to the pro-

visions and restrictions of the act of Congress." Culver became a stockholder in the bank, certificates having been issued to him as such, stating on their face the limitations on the power to transfer expressed in the by-law just referred to. By an agreement between Culver and the bank it was understood that his stock in the bank should secure the bank against any loss resulting from a deposit of its funds made by the bank with the house of Culver, Penn & Co., of New York, of which Culver was a member. When, however, this agreement was made the certificates of stock were not delivered to the bank, but remained in the possession of Culver. After the passage of the national bank act of 1864, Culver, in violation of his agreement with the bank, sold his stock and delivered the certificates thereof, with power to transfer the same to Lanier and Handy, who requested a transfer of the same. This the bank refused to do on the ground of Culver's agreement, and on the further ground of the provision in the by-law and certificates, which, it was asserted, but expressed by reference the provisions of the thirty-sixth section of the act of 1863. Two questions were necessary to be decided: a, the right of the bank resulting from the understanding with Culver; and, b, its right arising from the terms of the by-law and certificate. These questions were ruled adversely to the bank. It was held that the agreement between the bank and Culver was void because it was within the prohibitions of both the thirty-seventh section of the act of 1863 and the thirty-fifth section of the act of 1864, prohibiting a national bank from loaning on the security of its own capital stock, etc. Irrespective, however, of this question, it was expressly decided that, as the act of 1864 had repealed the provision of the act of 1863, subjecting transfers of stock in national banks to debts due by the stockholder to the bank, or permitting the board of directors to provide to that effect, the result of the act of 1864 was impliedly to prohibit a bank from imposing such a condition on the transfer of stock. And the doctrine was applied to a by-law adopted prior to the passage of the act of 1864, because it was held that the continued operation of such a by-law was prevented by the act of 1864, as the right to continue it was not saved by the proviso to the repealing clause of that act. It was pointed out that the provision of the act of 1864, making the stock of national banks transferable like other personal property, was a fundamental departure from the act of 1863, and was based on a rule of public policy initiated by the act of 1864, intended to afford facilities for the transfer of stock in national banks, and thereby to encourage investment in such stock. The same subject was considered in *Bullard v. Bank*, 18 Wall. 589. There a by-law and form of certificate, adopted after the enactment of the statute of 1864, reserving the right to refuse to transfer stock in a national bank where the stockholder was indebted to the bank, was again determined to be ultra vires, because in conflict with the act of 1864, and such a provision was decided to be inoperative even as against the assignee in bankruptcy of the stockholder. These

cases foreclose every question presented on this record. The cases have been frequently referred to approvingly. *Earle v. Carson*, 188 U. S. 42, and authorities there cited. The contention that, although the condition in the certificate was void, nevertheless it operated as a notice to the insurance company, and thereby deprived it of its right to compel the transfer of the stock, but asserts in another form that there was power, by the insertion of such a condition in the certificate of stock to deprive the stock of a national bank of its attribute of sale like any other personal property. The extension wholly ignores not only the text of the law, but the rule of public policy which the national bank act has been decided to embody.

*Affirmed.*³

WHITE v. SALISBURY.

1862. 33 Mo. 150.⁴

ACTION to recover damages from the defendants for their failure to deliver certain railroad stock which they had agreed to sell and deliver to the plaintiff. The answer of the defendants alleged that they had had the shares in question transferred on the books of the railroad company.

DRYDEN, Judge, delivered the opinion of the court.

The defendants, by the contract sued on, agreed to deliver to the plaintiff's testator, on or before the fifteenth of July, 1857, seven 77-100 shares of stock in the North Missouri Railroad Company. The main ground of controversy in the court below was as to what was required to be done by the defendants to comply with their engagement, the plaintiff maintaining that the delivery of certificates

³ In *Re Klaus* (1886) 67 Wis. 401, 29 N. W. 582, *held* that a by-law requiring the consent of all the stockholders to a transfer of shares is void as against public policy, even where all the parties had notice. Orton, J. said at p. 407: "When the law makes stock personal property it clothes it with all the incidents of personal property, and the owner has full dominion over it and may dispose of it at will." Cf. *McNulta v. Corn Belt Bank* (1894) 164 Ill. 427, 45 N. E. 954, 56 Am. St. 203.

In *Driscoll v. West Bradley & Cary Mfg. Co.*, (1874) 59 N. Y. 96, *held* that a corporation has no power, in the absence of a provision to that effect in its articles, (to create by by-law a lien upon its stock for debts of the owner to the company. At p. 105, Folger, J. said: "Now we do not assert that it is not possible to legally abridge this right (of transfer). There may be power given by statute so to do. There may be, in some cases, an agreement of the original stockholders, among themselves, by their articles of association, that such power shall exist."

In *Mohawk Nat. Bank v. Schenectady Bank* (1894) 78 Hun (N. Y.) 90, 60 N. Y. St. 510, 28 N. Y. S. 1100, *held* that a corporation may provide for a lien in its articles of incorporation, distinguishing the *Driscoll* decision, *supra*. And see *National Bank v. Watsontown Bank* (1881) 105 U. S. 217, 26 L. ed. 1039.—Eds.

⁴ Statement abridged. Portion of opinion omitted.—Eds.

of stock to his testator was essential; while it was insisted by the defendants that a transfer of the stock to him on the books of the company was what was necessary, and all that was requisite. We think the defendants' theory the correct one. The end the parties intended to accomplish was to confer upon the plaintiff's testator the title and ownership of the stock contracted for. The delivery of the certificates from one party to the other would leave the title to the stock just where it was before. The only effectual mode of transferring the title was by a transfer on the books of the company, and by that means only.

The eighth section of the amended charter of the North Missouri Railroad Company, (Sess. Acts of 1853, p. 325-6,) provides that, "when payment for the stock of any subscriber or stockholder shall be fully made, the president and directors shall deliver one or more certificates of such stock, signed by the president, and countersigned by the treasurer, under the seal of the company, to such subscriber or stockholder, for the number of shares belonging to him or her, which certificates shall be transferable in a book to be kept for that purpose by the company, and, when transferred, shall be delivered up to the president and directors and be cancelled, and new certificates be issued to the assignee." In the *Agricultural Bank v. Burr*, 11 Shepley (Me.) R. 263, shares of bank stock had been transferred to the defendant on the books of the bank, but no certificate of stock had been issued to him. The question arose whether he was a stockholder. Mr. Justice Shepley, in delivering the opinion of the court, says, "a person becomes legally entitled to shares so transferred to him upon the books of the bank. The certificate is but additional evidence of his titles." Same *Bank v. Wilson et al.* 273, is to the same effect. (*Ellis v. Essex Merrimack Bridge Co.*, 2 Pick. 243; *Chester Glass Co. v. Dewey*, 16 Mass. 94.) * * *

*Judgment affirmed. All concur.*⁵

COMMONWEALTH v. CROMPTON.

1890. 137 Pa. St. 138, 20 Atl. 417.⁶

ACTION by the Commonwealth to escheat the property of Alexander McNaughton, who died intestate and without issue or any known kindred. Mrs. Susan Crompton, the administratrix of McNaughton's estate, claimed that a bond and various railroad stocks did not belong to the estate, but had been given to her by the deceased as a gift during his lifetime. She adduced evidence that deceased, a

⁵ *Boatmen's Ins. & Trust Co. v. Able* (1871) 48 Mo. 136, *Accord. Cf. Brinkerhoff-Farris Trust & Savings Co. v. Home Lumber Co.* (1893) 118 Mo. 447, 24 S. W. 129.

See *Nanney v. Morgan* (1887) L. R. 37 Ch. Div. 346.—Eds.

⁶ Statement rewritten. Portion of opinion omitted.—Eds.

few months prior to his death, presented her with a box, telling her that she should take it and that it would be useful to her after his death; that she thereupon took the box and put it away; that, after McNaughton's death, she opened it for the first time and found that it contained the bond and shares in question. The jury found for Mrs. Crompton and the Commonwealth appealed.

OPINION, MR. JUSTICE MCCOLLUM:

The specifications of error call in question the jurisdiction of the court, the right of the appellee to traverse the inquisition, and the sufficiency of the evidence to establish a valid gift.

Proceedings to escheat the estate of a person who died intestate, without heirs or any known kindred, are governed by the statutes, and these allow any person in whose possession the goods and chattels are found to traverse the inquisition in the Court of Common Pleas. In this case, the Commonwealth seeks to escheat, as the property of Alexander McNaughton, deceased, certain goods and chattels in the possession of the appellee, who is the administratrix of his estate. That she may traverse the inquisition as administratrix cannot be doubted since the decision of this court in *Crawford v. Commonwealth*, 1 Watts 480. But, while she is described in the traverse as administratrix, she denies that the estate has any title to the property in question, and claims that she is the sole owner of it.

* * * * *

A gift needs no consideration to support it, yet in the present case there was a valuable one acknowledged by the donor, and impelling him to the action which is the subject of this controversy. For twenty-one years he lived in the family of the donee as a boarder, and had his washing and mending done there, and for these he promised to pay her. He was in poor health the last four years of his life, and required and received from her and her children considerate care and attention. He often manifested grateful appreciation of these services, and expressed a purpose to make compensation for them. In execution of this purpose, he delivered to her the box containing the government bond and the certificates of railroad stock. It is apparent from the evidence that he intended to make an absolute gift of these securities to her, and that he supposed the delivery, and the words accompanying it, invested her with the exclusive control and ownership of them. There remains for consideration the question whether the failure to make a formal written transfer of the securities to the donee, will defeat the purpose of the donor and give them to the commonwealth as an escheat.

It is now settled that a valid gift of non-negotiable securities may be made by delivery of them to the donee without assignment or indorsement in writing. This principle has been applied to notes, bonds, stock and deposit certificates, and life insurance policies. In *Pennsylvania*, *Wells v. Tucker*, 3 Binn. 366; *Lacey v. Lacey*, 7 Pa. 251, and *Madeira's App.*, 17 W. N. 202, are illustrations of and

rest upon it, and it has distinct recognition and approval in other deliverances of this court. In *Walsh's App.*, 122 Pa. 177, we refused to extend it to a depositor's bank-book, but acknowledged "that, in the case of notes and other instruments payable to order, a delivery accompanied by words importing a present absolute gift would invest the donee with the ownership of the fund." The bank-book was regarded as on the same footing as a book of original entries, and the mere delivery of it to the donee as insufficient to pass any title to the accounts appearing upon it. But "a certificate of deposit is a subsisting chose in action, and represents the fund it describes, as in case of notes, bonds, and other securities, so that delivery of it as a gift constitutes an equitable assignment of the money for which it calls:" *Baskett v. Hassel*, 107 U. S. 602. In the case last cited, Mr. Justice MATTHEWS, after an exhaustive examination of the authorities, said: "The point which is made clear by this review of the decisions on the subject, as to the nature and effect of a delivery of a chose in action, is, as we think, that the instrument or document must be the evidence of a subsisting obligation, and be delivered to the donee so as to vest him with an equitable title to the fund it represents and to divest the donor of all present control and dominion over it, absolutely and irrevocably, in case of a gift *inter vivos*, but upon the recognized conditions subsequent, in case of a gift *mortis causa*."

The shares of stock are choses in action, and the certificates evidence of the title to them: *Slaymaker v. Bank*, 10 Pa. 373. Why may not a delivery of the certificates, coupled with words of absolute and present gift, invest the donee with an equitable title to the stock, which the donor or a volunteer cannot successfully assail? A stockholder may clothe another with the complete equitable title to his stock without compliance with the forms printed by the corporation: *United States v. Vaughan*, 3 Binn. 394; *Commonwealth v. Wātmonth*, 6 Wh. 117; *Building Assn. v. Sendmeyer*, 50 Pa. 67; *Finney's App.*, 59 Pa. 398; *Water-Pipe Co. v. Kitchenman*, 108 Pa. 630.

As the gift in question was supported by a valuable consideration, and the instruments which represented the ownership of the donor in the subject-matter of the gift were delivered to the donee, we think she has a title to the securities which cannot be destroyed in a proceeding by the commonwealth to escheat them.

*Judgment affirmed.*¹

¹ *Larimer v. Beardsley* (1906) 130 Iowa 706, 107 N. W. 935; *Leyson v. Davis* (1895) 17 Mont. 220, 42 Pac. 775, 31 L. R. A. 429; *Bond v. Bean* (1904) 72 N. H. 444, 57 Atl. 340, 101 Am. St. 686; *Gilkinson v. Third Ave. R. Co.* (1900) 47 App. Div. (N. Y.) 472, 63 N. Y. S. 792; *First Nat. Bank v. Holland* (1901) 99 Va. 495; 39 S. E. 126, 55 L. R. A. 155, 86 Am. St. 898, *Accord*. *Pennington v. Gittings* (1830) 2 Gill & J. (Md.) 208; *Baltimore Retort & Fire Brick Co. v. Mali* (1885) 65 Md. 93, 3 Atl. 286, 57 Am. Rep. 304; *Matthews v. Hoagland* (1891) 48 N. J. Eq. 455, esp. 486-490, 21 Atl. 1054, *Contra*.

And *cf.* *Coffey v. Coffey*, (1899) 179 Ill. 283, 53 N. E. 590.—Eds.

NEW YORK & NEW HAVEN R. CO. v. SCHUYLER.

1865. 34 N. Y. 30, 78-86.*

THIS is an action in the nature of a suit in equity, against Robert Schuyler and several hundred other defendants. The complaint was sustained by this court on demurrer, as will appear by reference to the reported case in 17 N. Y. 592. The object of the complaint was to have a large number of alleged false and fraudulent certificates and transfers of pretended stock of the company, made by Schuyler, and charged to be held by the defendants, adjudged spurious and void; and to compel the certificates to be brought into court and canceled; and to enjoin the several defendants from further prosecuting actions then pending, and from bringing suits against the company to enforce such certificates and transfers, or to recover damages for any reasons connected therewith.

DAVIS, J. * * *

There is still another class whose claims arise upon other facts, and rest on different principles. It is composed of those defendants who have received certificates representing actual and genuine stock of the company, but whose certificates were rendered valueless by a subsequent transfer to bona fide purchasers of the same stock, by the party to whose credit it stood on the books. To this class belong a part of the certificates held by the defendant Vanderbilt; the certificates of Jacob Surget, those of Ketchum & Bement, a part of Schuchard & Gebhard's, and perhaps some others. These certificates have been held to be spurious, by which I understand the court to mean nothing more than that they became invalid as representatives of stock, after the same stock had got into the hands of other bona fide holders.

The case of Jacob Surget presents the question arising in this class, with distinctness. On the 11th of December, 1852, he loaned to R. & G. L. Schuyler the sum of \$11,000, to secure which they delivered to him a certificate for 110 shares of the capital stock of the New York and New Haven Railroad Company issued to them with the ordinary assignment and blank power of attorney indorsed thereon and duly executed by them. On the 2d of September, 1853, Surget loaned to that firm the further sum of \$9,500, on the security of 110 other shares of such stock, the certificate for which was delivered to him with the proper assignment and power of attorney executed in blank by said firm. These certificates were genuine, and represented actual stock of the company then owned by the Schuylers and standing to their credit on its books.

On the 3d of November, 1853, Surget was, and had been from September, 1850, the owner of 200 shares of the stock of the company, for which he held its certificate. On that day he agreed with

* Only a portion of the opinion is given.—Eds.

the Schuylers to sell to them this stock, and to loan them some \$7,000, in security for which he was to hold 75 shares of the stock thus sold to them. He made the loan, and, to carry out the arrangement, transferred to them the 200 shares, and delivered up his certificate, and at the same time received back a certificate for seventy-five shares issued to them at that time; with the proper and duly executed power of attorney. The stock represented by these several certificates was genuine, and no question is or can be made affecting the propriety or authority of the act of the officer in issuing the certificates.

Surget did not transfer the stock on the books, but retained the certificates in his possession, and his loans to the Schuylers remain for the most part unpaid. Afterwards, Schuyler & Co. transferred on the books all their stock to other parties, who were purchasers in good faith, and the outstanding certificates held by Surget were not surrendered nor accounted for.

In November, 1854, Surget presented his certificates at the transfer office of the company and offered to surrender them, and requested permission to transfer the stock represented by them; but the company refused to receive the surrender or permit the transfer, on the allegation that the certificates did not represent genuine stock.

The plaintiffs have demanded and obtained a judgment declaring the certificates held by Surget to be void, and directing their cancellation. By his answer, Surget insisted that his stock was, and should be declared to be, genuine, or that he should be awarded damages for the refusal of the company to recognize it as such.

The principal questions that present themselves in this case are:

First. Whether the subsequent purchasers in good faith of the stock acquired by the transfers on the books of the company a title superior to Surget's, under the certificates held by him; and,

Second. If they did, whether the company are liable to him for permitting the transfers to be made without the production and surrender of the outstanding certificates.

The law, as settled by authority, touching the first of these questions, is this: Where the stock of a corporation is by the terms of its charter or by-laws transferable only on its books, the purchaser who receives a certificate with power of attorney gets the entire title, legal and equitable, as between himself and his seller, with all the rights the latter possessed; but as between himself and the corporation, he acquires only an equitable title which they are bound to recognize and permit to be ripened into a legal title, when he presents himself, before any effective transfer on the books has been made, to do the acts required by the charter or by-laws in order to make a transfer. Until those acts be done he is not a stockholder and has no claim to act as such; but possesses, as between himself and the corporation, by virtue of the certificate and power, the right to make himself, or whomsoever he chooses, a stockholder, by the

prescribed transfer. The stock not having passed by the delivery of the certificate and power of attorney, the legal title remains in the seller, so far as affects the company and subsequent bona fide purchasers who take by transfer duly made on the books. And hence a buyer in good faith, of the person in whose name the stock stands on the books, who takes a transfer in conformity to the charter or by-laws, permitted to be made by the authorized officer of the corporation, becomes vested with a complete title to the stock, and cuts off all the rights and equities of the holder of the certificate to the stock itself. What other rights and equities he may possess is another question; but if the transferee has taken in good faith and for value, the stock is gone beyond his reach and beyond recall by the corporation. (*Stebbins v. Phenix Fire Ins. Co.*, 3 Paige, 350; *Union Bank v. Laird*, 2 Wheat., 390; *Angell & Ames on Corp.*, 352, 353, 3d ed.; *Mechanics' Bank v. New York and New Haven R. R. Co.*, 3 Kern., 621, et seq., per Comstock, J.; *Bank of Utica v. Smalley*, 2 Cow., 770; *Gilbert v. Manchester Iron Co.*, 11 Wend., 627; *Bargate v. Shortridge*, 31 Eng. L. and Eq., 58; *Wilson v. Little*, 2 Comst., 447, per Ruggles, J.)

The non-production and surrender of the certificate at the time of the transfer, is not fatal to the title of the transferee. It is only essential to the safety of the corporation, and may be waived by it at its own peril. The company has the means of knowing whether a certificate of particular stock is outstanding or not, and the power to compel its return and cancellation before any transfer is made, and a buyer, where the transfer is permitted by the corporation to be made on its books, by one to whose credit the stock is standing, has a right to presume that no certificate has issued, or if one has, that his vendor has duly surrendered it for cancellation.

It follows, therefore, that the stock represented by the certificates in Surget's hands, passed to the subsequent bona fide transferees; and the company had neither the power nor right to permit it to be transferred to Surget on his subsequent demand. In my judgment, no action would lie against them for that refusal. It was, in effect, asking them to do what the law prohibited them from doing—to duplicate the shares represented by the certificates, with a knowledge that they had long before passed into other hands, where they were still in actual and potential existence. The rights of Surget, if he have any, must stand on other grounds than the refusal in November, 1854, to permit him to transfer stock which then legally belonged to others.

The second question is, whether the company are liable for permitting the transfers to be made, without the production and cancellation of the outstanding certificates, whereby Surget's equitable rights to the stock were cut off and lost. The question is first to be considered on the assumption that the company permitted the transfer. It has been seen that Surget's rights as between himself and the corporation were those of an equitable, and not legal, owner

of the stock. It may be stated as a clear proposition, that where notice of the rights of an equitable owner are brought home to a party to be affected by such rights, the remedies for a subsequent injury to those rights is complete and perfect; and so it cannot be doubted, that if Surget had given the company actual and plain notice that he was the holder and owner of the certificates in his hands, the permitting of a subsequent transfer to another, under circumstances that caused the title of the stock to be lost to him, would have subjected the corporation to respond to him for the injury. But the company had not actual notice; and hence it is essential in this view of the question, to show that its relations to the holder of the certificates were equivalent to those of a party with notice. By its charter the corporation was authorized to make by-laws to regulate the transfer of its stock. It had done this by the adoption of by-laws, which, as we have seen, *ex proprio vigore*, prevented the legal title of stock from passing otherwise than by the prescribed mode of transfer; and as a part of these by-laws it had provided for the issuing of certificates to stockholders, in a form to be "appointed and directed" by the directors; had authorized transfers by power of attorney, and had expressly declared that when a certificate of stock had been issued to a stockholder, no transfer of the stock should thereafter be permitted without the surrender of said certificate. The board of directors had also prescribed a form of certificate which was thereafter invariably used, which declared that the stockholder was entitled to the number of shares named, and that they were transferable on the books of the company at the office named, "on the surrender of this certificate." They prepared and caused to be printed on the back of this form of certificate, an assignment thereof, with a power of attorney to be executed in blank by the stockholder, for the purpose of facility of transfer. That this was a customary and long-established mode of making stock readily and profitably marketable, was well known to the company, for its by-laws speak of it as "the usual form". Now while the corporation could not give to a certificate of this kind, *negotiability* in its legal commercial sense, it could and did approximate to that characteristic, as nearly as legally possible, for the purpose of making its stock more valuable by the ease with which its certificates could pass from hand to hand by simple delivery. It was never intended to lock up those instruments in the hands of the stockholders named in them—but to give to them every practicable facility as the basis of commercial transactions. And this was legitimate and proper, since it tended to enhance the value of the corporate franchise, by making its stock a subject of easy investment and ready convertibility. But it was essential to make these certificates in a form to secure public confidence, and this could only be done by making them *solemn assurances of rights*. Hence, by its by-laws, the corporation declared that the stock represented by them should never be transferred, except upon the delivery and cancellation of

the certificate; and this provision, in effect, it embodied in the certificate itself. Armed with such instruments, it sent its stockholders into the commercial world, with knowledge of the established usage of dealing on the faith of such certificates; and it addressed them, not to the stockholder himself, who had no need of the notice, but to all men who should desire to participate in the advantages or profits of its franchise. It was to all such persons that it assured safety in purchasing the certificate, by declaring that the stock should only be transferred upon its surrender and cancellation. In this manner it courted and established privity between itself and every holder of the certificate, by asserting that his equitable title was safe, because nobody but he could transfer the legal title. It should be constantly borne in mind, that the certificate now spoken of is a valid one, representing actual stock; and upon the transfer of such an one, a privity at once springs up, upon the title he acquires from his vendor, and his equities as against the corporation, through which every assurance of the instrument is addressed to him; and it is upon this principle that *Kortright v. Buffalo Commercial Bank* (22 Wend. 348), properly stands. When, therefore, the original stockholder to whom such a certificate has been issued, comes to the corporation to transfer the stock, its books are notice to it that the certificate has been issued. The by-laws and the certificate are notice that it must be surrendered before the stock can be transferred, and its non-production is notice that it is not in possession of the party claiming to transfer. These facts operate as notice that some other party is its owner; and they put the corporation upon the inquiry that would lead ordinary sagacity to the truth; and this is equivalent in equity to actual notice of all the rights that inquiry might develope. * * *

In *Pollock v. The National Bank* (3 Seld., 274), it was held that where a bank had permitted the transfer of stock under a forged power of attorney, and canceled the original and issued a new certificate, the bank was liable to the real owner to replace his stock or pay him the value thereof. In that case there was undoubted good faith in the bank, the officers of which had been deceived by a forgery into doing the act which had produced the injury. In this case the assent could not have been in good faith, for it was in violation of an inherent law of the company's stock regulations, and no milder rule of liability could flow from it. (*Davis v. Bank of England*, 2 Bing., 393; *Ashby v. Blackwell*, 2 Eden Ch., 299.)

But there is another and well-settled principle upon which a corporation that permits a transfer of stock under such circumstances should be held liable. It is this, that "all duties imposed upon a corporation by law raise an implied promise of performance" (Per NELSON, J., *Kortright v. Buffalo Commercial Bank*, 20 Wend. 91-94.) It was upon this principle that assumpsit was maintained in the case just referred to, and that Lord MANSFIELD denied a mandamus in *The King v. The Bank of England* (Doug., 523), to

compel the bank to enter a transfer of stock on its books, on the ground that an action would lie for a complete satisfaction equivalent to specific relief. "The law supposes that the corporation promises or undertakes to do its duty, and subjects it to answer in a proper action for its defaults, whether of nonfeasance or misfeasance." (3 Dane, 109; 5 id., 160.)

In *Bank of Columbia v. Patterson* (7 Cranch, 299, pp. 305, 306), Mr. Justice STORY, in an able, learned and concise statement of the powers, duties and liabilities of corporations, observed, that "all duties imposed on them by law, and all benefits conferred at their request, raise implied promises for the enforcement of which an action may well lie." PUTNAM, J., in *Sargeant v. Franklin Ins. Co.*, 8 Pick., 98.)

The action of assumpsit was brought in *Kortright v. The Buffalo Commercial Bank*, for a refusal to permit a party holding a certificate and power of attorney to transfer the stock on the books of the bank. It was held, for the purpose of sustaining that form of action, that the law imposed the duty to permit the transfer, and raised an implied promise in favor of the party holding the certificate that that duty should be performed. In this case it was a duty enjoined upon the corporation by its by-laws not to permit a transfer of the stock without the surrender and cancellation of the certificate which it has issued. That duty raises a promise in favor of the holder of the certificate that it shall not be done. On the face of the certificate is a notice to all parties that the instrument must be surrendered upon making a transfer, and I think it would be straining no principle of law to say, that the contents of the certificate are an assurance amounting to a promise that this rule shall be adhered to for the benefit of the equitable owner of the stock. The court went much farther in the *Bridgeport Bank* case, and held that "The *bona fide* holders of such certificates had a right to rely on the certificates, under the circumstances, as securing to them the stock which they represented against all transfers to other parties." (30 Conn., 270.)

If the corporation, therefore, permitted the transfer of the stock, of which Surget was the equitable owner, in violation of its undertaking to protect his rights, the law gives him a remedy to the extent of the injury, upon the implied promise to do no such act to his prejudice.*

* Cf. *Robinson v. National Bank* (1884) 95 N. Y. 637. See *Société Générale De Paris v. Walker* (1886) L. R. 11 App. Cas. 20; *Rainford v. James Keith & Blackman Co., Lim.* (1904), L. R. (1905) 1 Ch. Div. 296; *Peat v. Clayton* (1906) 1 Ch. Div. 659; *Machinists' Nat. Bank v. Field* (1878) 126 Mass. 345; *Allen v. South Boston R. Co.* (1889) 150 Mass. 200, 22 N. E. 917, 5 L. R. A. 716, 15 Am. St. 185; *Brisbane v. Delaware, L. & W. R. Co.* (1883) 94 N. Y. 204.

In *Fifth Avenue Bank v. Forty-second Street & G. St. Ferry R. Co.* (1893) 137 N. Y. 231, 33 N. E. 378, 19 L. R. A. 331, 33 Am. St. 712, held that damages could be recovered in an action in tort against a corporation for a refusal

CHEMICAL NATIONAL BANK v. COLWELL.

1892. 132 N. Y. 250, 30 N. E. 644.

APPEAL from judgment of the General Term of the Court of Common Pleas for the city and county of New York, entered upon an order made February 10, 1890, which affirmed a judgment in favor of plaintiff entered upon a verdict directed by the court.

This action was brought against defendants as directors of the New York Lumber Auction Company (Limited) to recover an indebtedness of the company because of failure on their part to file an annual report.

The material facts are stated in the opinion.

PARKER, J.—The debt which lies at the foundation of the judgment under review is alleged by the plaintiff to have been incurred by the "New York Lumber Auction Company (Limited)," a corporation organized pursuant to chapter 611 of the Laws of 1875. The corporation has no money with which to pay the obligation, and the assertion of defendant's liability to respond therefor is based on the default of the corporation in making the annual report required by statute.

The defendant's denial of liability is placed on three grounds:

1. That the note having been made by the corporation payable to its own order, the plaintiff by discounting it for the personal benefit of Jones, a director and secretary and treasurer of the company, became burdened with the necessity of proving that the note was issued for the benefit of the corporation making it, which it failed to do.

2. That the defendant resigned as director November 5, 1885, and before the arrival of the time for making the annual report in respect to which default was made.

3. That before the time came to make the report the defendant had ceased to be a stockholder, and, therefore, by operation of the statute, had ceased to be a director.

As we have reached the conclusion that the last position is well

on its part to issue stock, although the corporation had already issued all the stock that it was authorized to issue.

In *Allen v. South Boston R. Co.*, *supra*, held, at p. 207, that damages should be assessed on the basis of the market value of the stock at the time of the first refusal to transfer, and that the same rule applies to both genuine and spurious or unauthorized stock.

In *McLean v. Wright Medicine Co.* (1893) 96 Mich. 479, held that in an action to recover damages against defendant corporation for a refusal to transfer stock to him upon the books of the company, plaintiff was entitled only to nominal damages because he had not been deprived of his stock, and as holder of the endorsed certificate, was the absolute owner, possessed the evidence of title, had the right to attend meetings and to share in the profits, and, in fact, "was entitled to all the rights of every other stockholder." But see *Protection Life Ins. Co. v. Osgood* (1879) 93 Ill. 69.

See *Johnston v. Laffin* (1880) 103 U. S. 800, 26 L. ed. 532.—Eds.

taken and calls for a reversal of the judgment, the other questions will not be considered.

The corporation was created in July, 1885; the annual report omitted should have been made within twenty days after the 1st day of January, 1886, and the note in suit bears date July 2, 1886. The defendant was one of the subscribers to the capital stock of the company, and was elected a director. Subsequently he informed Jones, the secretary and treasurer of the corporation, that he wished to resign all connection with the company, assigning as a reason the duties imposed by the executorship of his father's estate.

After several conversations of the same general character, and on November 5, 1885, he, accompanied by his co-executor, Mr. Milne, went to the office of the company, and met Jones, the secretary and treasurer, and a Mr. Atchison, an employé. The defendant asked for his stock and received a certificate for eighty shares, which he indorsed as follows:

"For value received, I hereby sell, transfer and assign to Latimer E. Jones, eighty shares of stock within mentioned, and authorize L. E. Jones to make the necessary transfer on the books of the company.

"Witness my hand and seal this 5th day of November, 1885.

"In presence of

A. W. COLWELL.

T. S. ATCHISON."

After executing this assignment he gave the stock certificates to Jones, at the same time saying: "Now, Jones, that severs all my connection with the Lumber Auction Company; I have got nothing further to do with it; you have got father's stock, he is dead, and that settles that, and I have given you mine, and that clears up all that, and I have nothing further to do with the company."

Jones accepted the stock and the defendant asked for the transfer-book, but the company did not have one, and he was told that it was not necessary. Some days later a transfer-book was obtained and the stock transferred, but as Jones, at the suggestion of Atchison, issued a new certificate to himself for seventy-five shares, and to the defendant, but without his knowledge, for the remaining five shares, and a few days later induced him to accept it, but not with the understanding that he should be a director, we are led to inquire whether the defendant did not cease to be a stockholder on the fifth of November?

The importance of that inquiry rests in the requirement of the statute that the directors "at their election, and throughout their terms of office shall be stockholders in such corporation, to at least the extent of five shares." If then defendant ceased to be a stockholder in the corporation on November fifth, the statute put an end to his official relation with the company. It should be observed that on the occasion of the assignment of the stock to Jones and his acceptance thereof, it was understood to be an absolute disposition of all the defendant's shares. The subsequent issue of five shares to

him was not in pursuance of any understanding had at the time of such assignment and was done at the instance of Atchison, who made out the certificate and suggested to Jones that he persuade Colwell to accept it.

The consideration of the undisputed testimony to which we have referred is not embarrassed by any question as to the good faith of the defendant or the propriety of his action. The corporation was solvent when he sought to terminate his relation with it as a stockholder and director, and the indebtedness which induces this controversy was created months afterward. That he intended to make an effectual transfer of his stock is not questioned; nor is it asserted that he omitted to do anything which the situation permitted to effectuate his purpose. The contention is that he did not accomplish his desire because the transfer was not made on the books of the company that day.

He sought to have that done, but it was not, because the company had failed to provide books for the purpose, as provided by its by-laws. ~~It has been frequently held that such provisions are intended solely to protect the corporation, and do not operate to prevent the passing of the entire title, legal and equitable, in the shares, as between the parties, by the delivery of the certificate, with assignment and power of transfer.~~ (Isham v. Buckingham, 49 N. Y. 216; Robinson v. National Bank of New Berne, 95 id. 637; McNeil v. Tenth National Bank, 46 id. 331; Leitch v. Wells, 48 id. 585.)

The plaintiff's contention then is reduced to the position that notwithstanding the defendant parted with all title, both legal and equitable, in the shares, he still continued to be a stockholder within the meaning of the statute, because through the neglect of the corporation in providing proper transfer-books, the stock was not formally transferred on its books.

We do not think the statute should receive such a construction. The requirement that a director should have, at his election, and throughout his term of office, at least five shares, manifests that it was the policy of the legislature that the management of the affairs of such corporations should only be committed to those having a personal pecuniary interest in its success or failure, in the conduct of business for which it was created; otherwise the provision is without reason for its support.

It would seem to follow that as soon as a director parts with all beneficial interest in, and control over, the stock which he is required to hold, and causes the officers of the corporation to have knowledge of such fact by a request that a proper transfer be made on the books of the company, he no longer possesses the qualifications which the statute declares to be essential.

If the defendant had not been elected a director at the first election, and had simply subscribed for eighty shares of stock it would

hardly be contended that after making the disposition of it, which he did on November fifth, that he would have been eligible to the position of director; nor would there have been any excuse for assuming that he was, for even the books of the company did not show an apparent eligibility; there were no transfer-books, and the only evidence there was on that subject, in the possession of the company, showed that the defendant had parted with all interest in and dominion over the stock for which he had subscribed.

For the same reason, the statute executing itself operated to divest him of title to the office which he had ceased to be qualified to hold.

In the cases cited by the respondent, the question presented for our determination was neither before the court nor decided, and as they have received consideration by this court in *Cutting v. Damerel* (88 N. Y. 410), they need not be further alluded to in this connection.

The judgment should be reversed.

BRADLEY, J. (dissenting).—I do not see my way to concurrence in reversal of the judgment.

The purpose of the defendant to resign his position of director of the N. Y. Lumber Auction Co. (Limited), was not brought to the attention of the board of directors. And his statement made to that effect to Jones, who was the secretary-treasurer of the company, does not seem effectual to accomplish it.

The statute under which the company was incorporated provides that the members of the board of directors at their election, and throughout their term of office, shall be stockholders in such corporation to at least five shares and shall hold their offices until their successors are chosen. (L. 1875, ch. 611, § 10.) In view of that provision of the statute the question arises whether the transfer by a director of his stock operates to terminate his relation as such to the company, and if so whether the defendant did effectually for that purpose transfer his stock prior to the creation of the debt upon which the action is founded.

My attention has been called to no other provision of the statute upon the subject of the eligibility of a person for the place of director. And that does not in terms declare that such relation shall terminate when he ceases to be a stockholder. The defendant was such when elected and the statute provided for his retirement only on the election of his successor. But without further considering that question, the inquiry arises, Did the plaintiff, as between him and the company cease to be a director before such debt was contracted? By reference to the statute it is seen that "no transfer of stock shall be valid for any purpose whatever, except to render the person to whom it shall be transferred liable for the debts of the corporation according to the provisions of the act, until it shall have been entered" in the book referred to "by an entry showing from and to whom transferred." (Id. § 17.) And the by-law of the company provided that transfers of shares should "only be made upon the books of the com-

pany" in the manner there directed. The defendant owned eighty shares of the stock, and no more than seventy-five of them were transferred upon the books of the company, and as between him and it, his relation of stockholder of five shares continued. (*Adderly v. Storm*, 6 Hill, 624; *Worrall v. Judson*, 5 Barb. 210; *Rosevelt v. Brown*, 11 N. Y. 148.)

It would seem that the question here is not in the fact whether the defendant had transferred his stock so as to vest title to it in another, as between them, * * * as it is between him and the corporation that the inquiry would arise whether or not he continued to be one of its directors. And for the purpose of his eligibility he would properly be treated by the company as a stockholder until his transfer was entered on the book. If that view is sound, he never, as to the company, ceased to have five shares of the stock after he was elected director.

While it is true he made and delivered to Jones the certificate with an assignment upon it covering the eighty shares without consideration, it appears that when the certificate was surrendered and new ones taken the shares were so divided that Jones took seventy-five, and certificate for the other five was issued to the defendant. All inferences of fact legitimately arising from such transaction and bearing in that direction are to be taken in support of the recovery.

These suggestions lead to the conclusion that the judgment should be affirmed.

All concur with PARKER, J., except BRADLEY, J., dissenting.

*Judgment reversed.*¹⁰

WEBSTER v. UPTON.

1875. 91 U. S. 65, 23 L. ed. 384.¹¹

ERROR to the Circuit Court of the United States for the Northern District of Illinois.

The facts are stated in the opinion of the court.

MR. JUSTICE STRONG delivered the opinion of the court.

The Great Western Insurance Company, of which the plaintiff below is the assignee in bankruptcy, was incorporated under the laws of Illinois in 1857, with general power to insure all kinds of property against both fire and marine losses. Subsequently to its organization, its capital was increased to more than \$1,000,000, and it was authorized by law further to increase its capital to \$5,000,000. It does not appear, however, from the record, that,

¹⁰ Cf. *Perkins v. Lyons* (1900) 111 Iowa 192, 82 N. W. 486; *Man v. Boykin* (1908) 79 S. Car. 1, 60 S. E. 17 (company neglected to register and transferer's liability as a stockholder held to continue).

See also *Robinson v. National Bank* (1884) 95 N. Y. 637.—Eds.

¹¹ Portions of opinion omitted.—Eds.

of the stock subscribed, more than about \$222,000 was ever paid in,—a sum equal to nearly twenty per cent. of the par value,—leaving over \$965,000 of subscribed capital unpaid. In this condition the company went into bankruptcy in 1872, owing a very large sum, equal to if not greater than its entire subscribed capital; and Clark W. Upton, the plaintiff, become the assignee. The District Court then directed a call to be made for the eighty per cent. remaining unpaid of the capital stock. A call was accordingly made; and, payments having been neglected, the assignee brought this suit against the defendant, averring that he was the holder of one hundred shares, of the par value of one hundred dollars each, and, as such, responsible for the eighty per cent. unpaid. On the trial, evidence was given tending to show that one Hale was the owner of a large amount of stock of the company, for which he held the company's certificates; and that he had, through his brother, sold one hundred shares to the defendant, on which twenty per cent. had been paid. The books of the company had been destroyed in the great fire in Chicago in 1871; but there was evidence tending to show that the defendant's name was on the stock ledger, (and that the defendant transferred, or caused the stock bought from Hale to be transferred to himself on the books of the company.) The district judge submitted to the jury to find whether the defendant actually thus became a stockholder, recognized as such on the books of the company; instructing them, that, if he did, he was liable for the eighty per cent. unpaid as if he had been an original subscriber. A verdict and judgment having been recovered by the plaintiff, the case was removed by writ of error to the Circuit Court, where the judgment was affirmed; and the judgment of affirmance we are now called upon to review. * * *

But, if the law implies a promise by the original holders or subscribers to pay the full par value when it may be called, it follows that an assignee of the stock, when he has come into privity with the company by having stock transferred to him on the company's books, is equally liable. The same reasons exist for implying a promise by him as exists for raising up a promise by his assignor. And such is the law as laid down by the text-writers generally, and by many decisions of the courts. *Bond v. The Susquehanna Bridge*, 6 Har. & J. 128; *Hall v. United States Insurance Company*, 5 Gill, 484; *Railroad Company v. Boorman*, 12 Conn. 530; *Haddersfield Canal Company v. Buckley*, 7 T. M. 36. There are a very few cases, it must be admitted, in which it has been held that the purchaser of stock partially paid, is not liable for calls made after his purchase. Those to which we have been referred are *Canal Company v. Sansom*, 1 Binn. 70, where the question seems hardly to have been considered, the claim upon the transferee having been abandoned; and *Palmer v. The Ridge Mining Company*, 34 Penn. St. 288, which is rested upon Sansom's case, and upon the fact, that, by the charter, the company was authorized to forfeit the stock for non-payment of calls.

We are also referred to *Seymour v. Sturgess*, 26 N. Y. 134, the circumstances of which were very peculiar. In neither of these cases was it brought to the attention of the court that the stock was a trust fund held for the protection of creditors in the first instance, a fund no part of which either the company or its stockholders was at liberty to withhold. They do not, we think, assert the doctrine which is generally accepted. In *Angell and Ames on Corporations*, sect. 534, it is said,—

“When an original subscriber to the stock of an incorporated company, who is so bound to pay the instalments on his subscription from time to time as they are called in by the company, transfers his stock to another person, such other person is substituted not only to the rights, but to the obligations, of the original subscriber, and he is bound to pay up the instalments called for after the transfer to him. The liability to pay the instalments is shifted from the outgoing to the incoming shareholder. A privity is created between the two by the assignment of the one and the acceptance of the other, and also between them and the corporation; for it would be absurd to say, upon general reasoning, that, if the original subscribers have the power of assigning their shares, they should, after disposing of them, be liable to the burdens which are thrown upon the owners of the stock.”

So in *Redfield on Railways*, 53, it is said the cases agree that whenever the name of a vendee of shares is transferred to the register of shareholders, the vendor is exonerated, and the vendee becomes liable for calls. We think, therefore, the transferee of stock in an incorporated company is liable for calls made after he has been accepted by the company as a stockholder, and his name has been registered on the stock books as a corporator; and being thus liable, there is an implied promise that he will pay calls made while he continues the owner. * * *

The last assignment of anything that can be assigned for error is, that the court charged the jury as follows: “The only question is, was the defendant a stockholder of the company? If the testimony satisfies you that the defendant purchased of Hale one hundred shares of this stock, and that it was transferred in the books of the company, either by Webster, the defendant, or by Hale, who sold the stock, or by the direction of either of them, then the defendant is liable the same as if he had subscribed for the stock.” The objection urged against this is that a transfer on the books directed by Hale, after the purchase by Webster, could not affect the latter’s liability. But, if Webster became the purchaser, it was his vendor’s duty to make the transfer to him, where only a legal transfer could be made,—namely, on the books of the company; and the purchase was in itself authority to the vendor to make the transfer.

Still further, it was Webster’s duty to have the legal transfer made to relieve the vendor from liability to future calls. A court of equity will compel a transferee of stock to record the transfer,

and to pay all calls after the transfer. 3 De G. & Sm. Ch. 310. If so, it is clear that the vendor may himself request the transfer to be made; and that, when it is made at his request, the buyer becomes responsible for subsequent calls. This, however, does not interfere with the right of one who appears to be a stockholder on the books of a company to show that his name appears on the books without right and without his authority.

*The judgment of the Circuit Court is affirmed.*¹²

SCOTT v. PEQUONNOCK NATIONAL BANK.

1883. 15 Fed. 494, 21 Blatchf. 203.¹³

THIS was an action at law to recover damages from the defendant corporation (a national bank organized under the laws of the United States relating to national banking, and doing business at Bridgeport, Fairfield County, Connecticut) for a refusal to allow a transfer upon its books, to the plaintiffs, of ten shares of its stock.

On the 20th day of May, 1868, the shares in question were registered on the books of the bank in the name of one Samuel Wilmot, and represented by a certificate in his name. On or about the 20th day of May, 1868, Wilmot assigned the shares to one Dunbar in the city of New York, by delivering to him the certificate therefor and a written assignment of and power of attorney to transfer the same; the assignment and power of attorney being in blank. Subsequently, and on or about January 1st, 1869, Dunbar assigned the shares to William B. Scott & Co., of New York City, by delivering to them the said certificate, written assignment and power of attorney. Subsequently, on the 13th of August, 1869, William B. Scott & Co. made demand upon the bank, at its place of business in Bridgeport, Fairfield County, Connecticut, to transfer the ten shares on the books of the bank to their own names and to issue a new certificate, at the same time presenting the old certificate in the name of Wilmot, together with the written assignment and power of attorney. The bank, however, refused to make the trans-

¹² *Brinkley v. Hambleton* (1887) 67 Md. 169, 8 Atl. 904; *Glenn v. Porter* (1896) 73 Fed. 275, 19 C. C. A. 503, *Accord*. In the first cited case, Alvey, C. J., said (p. 176): "The assignee takes the shares with all their rights and liabilities, so that if a liability to a loss has been incurred by the company before he purchased the stock, he may be called upon to contribute thereto as soon as he has accepted a transfer of the shares and become a shareholder in the concern. The liability to pay the calls made upon the stock after the transfer is shifted from the outgoing to the incoming shareholder; the transfer of stock working a complete novation of the contract of membership, the transferee being substituted to the place of the transferor, with all the rights and liabilities incident to the holding of the shares" (citing *inter alia*, the principal case).—Eds.

¹³ Statement rewritten.—Eds.

fer or to issue a new certificate, upon the ground that the said ten shares had, on the 26th day of July, 1869, been levied upon by virtue of a writ of attachment. Subsequently, on the 22nd day of October, 1869, the said ten shares were sold at public auction by the Sheriff of Fairfield County, Connecticut, pursuant to a judgment recovered (in the action in which the attachment had issued) against Wilmot on the 13th day of August, 1869, and an execution issued thereon on the first day of October, 1869, and the bank thereafter transferred the said shares upon its books from the name of Wilmot to the name of Clark, the purchaser at the sheriff's sale, and delivered to Clark a new certificate, and paid to him or his assigns the dividends accruing thereafter on said shares.

The bank had no by-laws, and the practice of the bank from its organization had been uniformly to require the transferor to authorize the transfer on the transfer books of the bank, either in person or by attorney, on the surrender of the outstanding certificate.

SHIPMAN, J.—This is an action at law to recover damages from the defendant corporation for a refusal to allow a transfer upon its books to the plaintiff of 10 shares of its stock. By written stipulation of the parties the case was tried by the court upon the hereto prefixed agreed statement of facts, and a jury was waived. Said facts are also found to be true. In the absence of a statute or of a provision in the charter, or of a by-law passed in pursuance of authority conferred by the charter, prescribing the exclusive manner in which the stock of a corporation shall be transferred, the stock-owner has a right to transfer such property to a purchaser by the delivery of the stock certificate, with a written assignment thereof. The title of a bona fide purchaser, to whom such certificate and assignment have been delivered, will not be divested by the subsequent attachment of the stock at the suit of a creditor of the vendor. *Boston Music Hall v. Cory*, 129 Mass. 435.

In some of the states statutes have been passed, or provisions have been inserted in the charters of the corporations, prescribing, either expressly or by implication, an exclusive method of transfer. The courts of Connecticut and Massachusetts have been quite rigid in maintaining the doctrine that when such statutes or charter provisions exist, an unrecorded transfer of stock shall not be valid as against attaching creditors of the vendor, and the courts of the former state have strongly leaned toward a construction of the charter of Connecticut corporations that shall compel a record of the assignment.

The Connecticut decisions, especially the earlier ones, which were made at a time when the rights of attaching creditors were strongly favored in that state, were to the effect that "in cases where the legislature in the act of incorporation either prescribe the mode of transferring stock, or authorize the company to do it in their by-laws, and the company do in their by-laws prescribe a mode as the only one to be pursued, that mode must be followed, or the legal title

will not pass by an assignment which would be good at common law had no particular and exclusive mode of transfer been prescribed." *Colt v. Ives*, 31 Conn. 25. The reason of the rule is stated by the court in *Colt v. Ives* as follows:

"In regard to chattels there must be a substantial change of possession accompanying and following the sale, or it will, unexplained, be conclusive evidence of fraudulent trust, which will render the sale void as to creditors. * * * And in the case of the purchase of stock in a corporation, there must be such a transfer of it as the legislature in the charter or by statute prescribed; and notice of the assignment of choses in action, and the transfer required by the statute of corporate stock, stand in lieu of the taking and retaining of the possession of personal chattels sold, being the only possession the nature of the property admits of."

In *Fisher v. Essex Bank*, 5 Gray 373, Chief Justice Shaw, after saying that whatever common-law rules, in the absence of any express rule of law, courts have adopted to determine what act constitutes the actual transfer of shares, when the transfer is so regulated such law must govern, held that an express provision in the act of incorporation of a bank that the stock should be transferable only at its banking house and on its books, made a transfer at the bank imperative as against an attaching creditor without notice of the previous assignment and delivery of the certificates to a purchaser. Judge Shaw's reasoning was to the effect that it is necessary to fix some act and some period of time at which the property changes and vests in the vendee, and that by the charter the transfer at the bank is made "the decisive act of passing the property—the legal, transferable, attachable interest."

The defendant claims the benefit of this series of decisions in the present case, and especially insists that as the defendant corporation is located in Connecticut the decisions of the courts of that state should have a controlling effect.

The defendant having been incorporated under the national banking act, the rules which regulate the transfers of its stocks are to be found in the statutes of the United States. The twelfth section of the act of 1864 (13 St. at Large, 102) provided that the shares of the stock of a national bank shall be "transferable on the books of the association in such manner as may be prescribed in the by-laws or articles of the association." In the eighth section of the same act the directors were empowered "to define and regulate by by-laws, not inconsistent with the provisions of the act, the manner in which its stock shall be transferred." These provisions are continued, in substantially the same terms, in sections 5135 and 5136 of the Revised Statutes. The construction of the statute, and the question of title as between the assignee and the attaching creditor are not controlled by the tenor of the decisions of any one state.

The construction which has been more generally placed upon those provisions in charters which require that the transfer shall be made

only upon the books of the corporation, or upon provisions of a similar character, is that this regulation is designed for the security of the bank and of bona fide purchasers who take transfers of the stock and possession of the certificates, without notice of any prior equitable transfer; and that, as between the parties to the sale, a transfer not in conformity to such provisions passes the equitable, though not the legal, title, and vests the right to the shares in the purchaser. *Black v. Zacharie*, 3 How. 483; *U. S. v. Cutts*, 1 Sumn. 133; *N. Y. & N. H. R. Co. v. Schuyler*, 34 N. Y. 80; *McNeil v. Tenth Nat. Bank*, 46 N. Y. 325. The New York decisions are to the effect that such a transfer conveys the legal title.

In *Johnston v. Laffin*, 103 U. S. 800, a case involving the transfer of shares in a national banking association, which, like the defendant, had made no by-laws on the subject of transfers of its stock, the court say:

"Shares in the capital stock of associations, under the national banking law are salable and transferable at the will of the owner. They are, in these respects, like other personal property. The statute recognizes this transferability, although it authorizes every association to prescribe the manner of their transfer. * * * It is not necessary, however, to consider what restrictions would be within its (the bank's) power, for it had imposed none. As between Laffin and the broker, the transaction was consummated when the certificate was delivered to the latter, with the blank power of attorney indorsed, and the money was received from him. As between them, the title to the shares then passed. Whether there be deemed a legal or equitable one, matters not; the right to the shares then vested in the purchaser. The entry of the transaction on the books of the bank, where stock is sold, is required, not for the translation of the title, but for the protection of the parties and others dealing with the bank, and to enable it to know who are its stockholders, entitled to vote at their meetings and receive dividends when declared. It is necessary to protect the seller against subsequent liability as a stockholder, and perhaps also to protect the purchaser against proceedings of the seller's creditors."

From this recent decision of the United States Supreme Court it appears that no exclusive method of transfer of stock in a national banking association is imposed by the provisions of the national banking act in regard to transfers, when no by-laws on the subject have been passed by the bank whose stock is in controversy, and that an unrecorded transfer is good as between the parties, and that the question of the rights of an attaching creditor to stock transferred by an unrecorded assignment, was regarded by the learned judge who wrote the opinion as one not definitely settled.

In holding that the unrecorded transfer has preference over the attachment, I am influenced by the following considerations:

First. In the absence of positive provisions of law or rules of evidence, either statutory or by decisions of courts, whereby trans-

fers of property, made without notice to the public or without registry, are declared fraudulent or void as against attaching creditors without notice, or whereby certain specified acts are made prerequisite to the vesting of a new title, creditors take their debtor's property subject to all honest and *bona fide* liens and equitable transfers. *Boston Music Hall v. Cory*, 129 Mass. 435; *Continental Nat. Bank v. Eliot Nat. Bank*, 7 Fed. Rep. 369. In this case there is no statutory provision, and no by-laws, which require that a transfer of the stock must be recorded, and, in the absence of such provision, the non-recording of the transfers is not evidential of fraud, as is the case when the vendor retains possession of chattels after a sale. The delivery of the certificate and the assignment and the power to transfer is a sufficient delivery at common law.

The statutes of Connecticut in regard to the attachment of stock and the levy of executions thereon, do not give to attaching creditors any peculiar right in stock which has been transferred by the unrecorded transfer. The extent of the rights which the attaching creditor would have in such stock of a Connecticut corporation is to be determined by other statutes than those which relate to attachment and levy of execution. *Boston Music Hall v. Cory*, 129 Mass. 435.

Second. The tendency of modern decisions is to regard certificates of stock attached to an executed blank assignment, and power to transfer, as approximating to negotiable securities, though neither in form or character negotiable. *Bank v. Lanier*, 11 Wall. 369; *Railroad Co. v. Bridgeport Bank*, 30 Conn. 270.

Third. The courts of these states, which have most strongly upheld the superior rights of attaching creditors of the vendor as against the unsecured equities of purchasers, regard the attaching creditor with less favor than formerly, "when attachments and sales on execution were the only compulsory mode of securing an appropriation of a debtor's property to the payment of his debts." *Colt v. Ives*, 31 Conn. 25.

Fourth. Decisions of high authority in the federal courts have given unrecorded transfers of stock for value precedence over subsequent attachments in behalf of creditors of the vendor, or over the claims of creditors. *U. S. v. Cutts*, 1 Sumn. 133, approving *U. S. v. Vaughan*, 3 Bin. 394; *Continental Nat. Bank v. Eliot Nat. Bank*, by Judge Lowell, 7 Fed. Rep. 369.

In the agreed statement of facts it is agreed that, if the plaintiffs are entitled to judgment, the amount of damages is the sum of \$1,030, plus the lawful interest on the same from August 13, 1869, to October 23, 1882. In an action of tort to recover unliquidated damages, if interest as a part of the damages is to be added to the principal sum found to be due, the rate of interest is now, in this state, 6 per cent. *Salter v. Railroad Co.*, 86 N. Y. 401.

Let judgment be entered for the plaintiffs in the sum of \$1,845.41, and costs of suit.¹⁴

✓

MCNEIL v. THE TENTH NATIONAL BANK.

1871. 46 N. Y. 325, 7 Am. Rep. 341.¹⁵

APPEAL from a judgment of the General Term, affirming a judgment, in favor of the plaintiff.

The action was brought, to compel the surrender to the plaintiff of 134 shares of the capital stock of the First National Bank of St. Johnsville, which had been acquired by the appellant in the following manner:

In November, 1866, the plaintiff then being the owner of the shares in question, had an account with Goodyear Brothers & Durant, of the city of New York, stock brokers, relating to other stocks, which they had purchased and were carrying for him. For the purpose of securing any balance which might become due them on that account, the plaintiff delivered to and left with them, the certificate of the 134 shares in dispute, with a blank assignment,

¹⁴ See also *Thurber v. Crump* (1887) 86 Ky. 408, 10 Ky. L. 59, 6 S. W. 145; *Lund v. Wheaton Roller Mill Co.* (1893) 50 Minn. 36, 52 N. W. 268, 36 Am. Rep. 623; *Haslam v. First Nat. Bank* (1900) 79 Minn. 1, 81 N. W. 535; *Doty v. First Nat. Bank* (1892) 3 N. Dak. 9, 14, 53 N. W. 77, 17 L. R. A. 259; and note in 16 Harv. Law Rev. 312, approving the principal case. But see *Ottumwa Screen Co. v. Stodghill* (1897) 103 Iowa 437, 72 N. W. 669; *Fisher v. Essex Bank* (1855) 5 Gray (Mass.) 373; *Shenandoah Valley R. Co. v. Griffith* (1882) 76 Va. 913. See notes, 9 Columbia Law Rev. 433, 9 Mich. Law Rev. 258, 11 id. 404.

In Alabama, Arkansas, Colorado, Connecticut, Indiana and New Mexico, the attachment creditor prevails (see *Cook on Corp's.*, 6th ed., sec. 490); also in California, if he has no notice, and in Iowa, unless notice has been served on the secretary of the corporation.

In Michigan, Minnesota, New Jersey, New York, Pennsylvania, Ohio, and some other states, the unregistered transferee prevails at common law. (*Cook*, sec. 487.) See *Flostroy v. Corby Coal Co.* (1912) 85 Atl. (N. J.) 578. So also, in New York, does the assignee of an ordinary chose in action at common law prevail over subsequent attaching creditors, and in cases of successive assignments the one first in time prevails. See *Williams v. Ingersoll* (1882) 89 N. Y. 508, at pages 522, 3; *Fortunato v. Patten* (1895) 147 N. Y. 277, at p. 283, 41 N. E. 572.

In Illinois, Maine, Maryland, Massachusetts, Virginia, Wisconsin, and some other states, the unregistered transferee is now protected by statute. (*Cook*, sec. 488). Cf. *People's Bank v. Gridley* (1879) 91 Ill. 457; *Atkinson v. Foster* (1890) 134 Ill. 472, 25 N. E. 528, and *Rice v. Gilbert* (1898) 173 Ill. 348, 50 N. E. 1087 (statutory intent to make corporate stock as nearly negotiable as possible); *Magerstadt v. Schaefer* (1905) 213 Ill. 351, 72 N. E. 1063. See also *Clews v. Friedman* (1903) 182 Mass. 555, 66 N. E. 201, holding that an unregistered transferee of the certificate gets a good title even as against a previous attaching creditor,—this by force of the statute.

And see *Mapleton Bank v. Standrod* (1904) 8 Idaho 740, 71 Pac. 119, 67 L. R. A. 656; *Lipscomb's Adm'r. v. Condon* (1904) 56 W. Va. 416, 107 Am. St. 938, with notes in 67 L. R. A. 656-684.—Eds.

¹⁵ Portions of opinion omitted.—Eds.

and power of attorney to transfer indorsed thereon, signed by the plaintiff, in the following words:

For value received, the undersigned hereby assigns and transfers unto * * * shares of the capital stock of the First National Bank of St. Johnsville, and do hereby constitute and appoint * * * true and lawful attorney, irrevocable for * * * and in * * * name and behalf, to make and execute all necessary acts of assignment and transfer required by the regulations and by-laws of said bank.

In witness whereof, I have hereunto set my hand and seal this — day of —.

(Signed.)

B. McNEIL.

Sealed and sworn in presence of —.

On the 18th of June, 1868, at the city of New York, the appellant at the request of Goodyear Brothers & Durant, paid the sum of \$45,135 to Fred. Butterfield, Jacobs & Co., receiving from them certain securities, including the certificate and power for the 134 shares in question, which had been previously pledged by Goodyear Brothers & Durant to Fred. Butterfield, Jacobs & Co.

Goodyear Brothers & Co. were at that time insolvent, and indebted to the appellant. In pledging the plaintiff's shares, they had acted without actual authority from him, and without his knowledge. He was indebted to them, on the account for which the shares were pledged to them, in the sum of \$3,000 with interest from December 1, 1866; but the account had not been rendered, or any demand made.

The appellant at the time of receiving the shares, had no knowledge of the plaintiff's interest therein.

The cashier of the appellant, within a few days after receiving the certificate, assignment and power, filled in the blank in the assignment and power with "I. H. Stout, cashier, Tenth National Bank, New York, one hundred and thirty-four," and dated the same the 19th day of June, 1868, and sent the scrip to the First National Bank of St. Johnsville, for the purpose of having the shares transferred on the books accordingly; but such transfer was prevented by an order of injunction in this action.

The plaintiff demanded of the appellant a surrender of the scrip, on payment of the balance due by him to Goodyear Brothers & Durant; which demand was refused.

The value of the shares was \$17,420. The balance of the advance made by the appellant thereon (\$45,135, less the proceeds of the other securities received therewith, \$29,915.19), was \$15,219.81, besides interest.

When the certificate and power came to the possession of the appellant, they bore the proper revenue stamp, duly cancelled with the stamp of Goodyear Brothers & Durant, and the name of Ch. Goodyear as subscribing witness to the power. The referee found, that when the plaintiff delivered them, they were not stamped or witnessed, and that the plaintiff had never authorized those acts.

The referee found in favor of the plaintiff, and in conformity with

his report, a judgment was entered, requiring the surrender of the scrip to the plaintiff, on payment by him of the \$3,000 and interest due by him to Goodyear Brothers & Durant.

This judgment was affirmed at General Term.

RAPALLO, J.—The pledge of the plaintiff's shares by his brokers, for a larger sum than the amount of their lien thereon, was a clear violation of their duty, and excess of their actual power. And if the effect of the transaction was merely to transfer to the appellant, through Fred. Butterfield, Jacobs & Co., the title or interest of Goodyear Brothers & Durant in the shares, the judgment appealed from was right.

It must be conceded, that as a general rule, applicable to property other than negotiable securities, the vendor or pledgor can convey no greater right or title than he has. But this is a truism, predicable of a simple transfer from one party to another where no other element intervenes. It does not interfere with the well-established principle, that where the true owner holds out another, or allows him to appear, as the owner of, or as having full power of disposition over the property, and innocent third parties are thus led into dealing with such apparent owner, they will be protected. Their rights in such cases do not depend upon the actual title or authority of the party with whom they deal directly, but are derived from the act of the real owner, which precludes him from disputing, as against them, the existence of the title or power which, through negligence or mistaken confidence he caused or allowed to appear to be vested in the party making the conveyance. (*Pickering v. Busk*, 15 East, 38; *Gregg v. Wells*, 10 Adol. & El., 90; *Saltus v. Everett*, 20 Wend., 268, 284; *Mowrey v. Walsh*, 8 Cow., 238; *Root v. French*, 13 Wend., 570.)

The true point of inquiry in this case is, whether the plaintiff did confer upon his brokers such an apparent title to, or power of disposition over the shares in question, as will thus estop him from asserting his own title, as against parties who took *bona fide* through the brokers.

Simply intrusting the possession of a chattel to another as depositary, pledgee or other bailee, or even under a conditional executory contract of sale, is clearly insufficient to preclude the real owner from reclaiming his property, in case of an unauthorized disposition of it by the person so intrusted. (*Ballard v. Burgett*, 40 N. Y. R. 314.) "The mere possession of chattels, by whatever means acquired, *if there be no other evidence of property or authority to sell from the true owner*, will not enable the possessor to give a good title." *Per* DENIO, J. in *Covill v. Hill* (4 Den., 323).

But if the owner intrusts to another, not merely the possession of the property, but also written evidence, over his own signature, of title thereto, and of an unconditional power of disposition over it, the case is vastly different. There can be no occasion for the delivery of such documents, unless it is intended that they shall be

used, either at the pleasure of the depositary, or under contingencies to arise. If the conditions upon which this apparent right of control is to be exercised, are not expressed on the face of the instrument, but remain in confidence between the owner and the depositary, the case cannot be distinguished in principle, from that of an agent who receives secret instructions qualifying or restricting an apparently absolute power.

In the present case, the plaintiff delivered to and left with his brokers, the certificate of the shares, having indorsed thereon the form of an assignment, expressed to be made "for value received," and an irrevocable power to make all necessary transfers. The name of the transferee and attorney, and the date, were left blank. This document was signed by the plaintiff, and its effect must be now considered.

It is said in some English cases, that blank assignments of shares in corporations are irregular and invalid; but that opinion is expressed in cases where the shares could only be transferred by deed under seal, duly attested, and is placed upon the ground that a deed cannot be executed in blank.

Without referring to the American doctrine on that subject, it is sufficient to say that no such formality was requisite in this case. It was only necessary to a valid transfer as between the parties, that the assignment and power should be in writing. The common practice of passing the title to stock by delivery of the certificate with blank assignments and power, has been repeatedly shown and sanctioned in cases which have come before our courts. Such was established to be the common practice in the city of New York, in the case of the New York and New Haven Railroad Company v. Schuyler (34 N. Y., 41), and the rights of parties claiming under such instruments were fully recognized in that case. And in the case of Kortright v. The Commercial Bank of Buffalo (20 Wend., 91, and 22 Wend., 348), the same usage was established as existing in New York and other States, and it was expressly held that even in the absence of such usage, a blank transfer on the back of the certificate, to which the holder has affixed his name, is a good assignment; and that a party to whom it is delivered is authorized to fill it up, by writing a transfer and power of attorney over the signature.

It has also been settled, by repeated adjudications, that, as between the parties, the delivery of the certificate, with assignment and power indorsed, passes the entire title, legal and equitable, in the shares, notwithstanding that, by the terms of the charter or by-laws of the corporation, the stock is declared to be transferable only on its books; that such provisions are intended solely for the protection of the corporation, and can be waived or asserted at its pleasure, and that no effect is given to them except for the protection of the corporation; that they do not incapacitate the shareholder from parting with his interest, and that his assignment, not on the books, passes the entire legal title to the stock, subject only to such liens

or claims as the corporation may have upon it, and excepting the right of voting at elections, etc. (Angell and Ames on Corporations, 8th ed., § 354; Bank of Utica v. Smalley, 2 Cow., 770; Gilbert v. Manchester Co., 11 Wend., 627; Kortright v. Com. Bank of Buffalo, 22 Wend., 362; N. Y. and N. H. R. R. Co. v. Schuyler, 34 N. Y., 80.)

In the case of Kortright v. Com. Bank, Chancellor WALWORTH, in a dissenting opinion, strenuously maintained, in conformity with his previous decision in Stebbins v. Phoenix Ins. Co. (3 Paige, 356), that by a transfer not on the books, the transferee acquired only an equitable right to or lien on the shares; and that, having but an equitable right or lien, he took subject to all prior equities which existed in favor of any other person from whom such assignment was obtained. (22 Wend., 352, 353, 355.) But his view was overruled by the majority of the court. The action was at law in assumpsit, brought by the holder of the certificate and power, for a refusal to permit him to make a transfer on the books, and the question of his legal title was necessarily involved in the case. The judgment therein must therefore be regarded as a direct adjudication that, as between the parties, the legal title to the shares will pass by delivery of the certificate and power. (See 20 Wend., 362.)

This was reasserted in this court in the New Haven Railroad Case (34 N. Y., 80), notwithstanding what was said in the Mechanics' Bank Case (13 id., 625).¹⁶

By omitting to register his transfer, the holder of the certificate and power fails to obtain the right to vote, and may lose his stock by a fraudulent transfer on the books of the company, by the registered holder, to a *bona fide* purchaser (34 N. Y., 80); but in this respect he is in a condition analogous to that of the holder of an unrecorded deed of land, and possesses a no less perfect title as against the assignor and others. And he would have an action against the corporation, for allowing such a transfer in violation of his rights. (Id.) He also takes the risk of the collection of dividends by his assignor, or of any lien the corporation may have on the shares. But in other respects his title is complete.

The holder of such a certificate and power, possesses all the external *indicia* of title to the stock, and an apparently unlimited power of disposition over it. He does not appear to have, as is said in some of the authorities cited, concerning the assignee of a chose in action, a mere equitable interest, which is said to be notice to all persons dealing with him that they take subject to all equities, latent or otherwise, of third parties; but, apparently, the legal title, and the means of transferring such title in the most effectual manner.

Such, then, being the nature and effect of the documents with which the plaintiff intrusted his brokers, what position does he occupy toward persons who, in reliance upon those documents, have in good faith advanced money to the brokers or their assigns on a

¹⁶ Cf. East Birmingham Land Co. v. Dennis (1888) 85 Ala. 565, 567, 5 So. 317, 2 L. R. A. 836, 7 Am. St. 73, commenting on these decisions.—Eds.

pledge of the shares? When he asserts his title, and claims, as against them, that he could not be deprived of his property without his consent, cannot he be truly answered that, by leaving the certificate in the hands of his brokers, accompanied by an instrument bearing his own signature, which purported to be executed for a consideration, and to convey the title away from him, and to empower the bearer of it irrevocably to dispose of the stock, he in fact "substituted his trust in the honesty of his brokers, for the control which the law gave him over his own property," and that the consequences of a betrayal of that trust, should fall upon him who reposed it, rather than upon innocent strangers from whom the brokers were thereby enabled to obtain their money?

These principles, in substance, were applied in the case of Kortright v. The Commercial Bank. But it is sought to distinguish that case from this; and it is argued, that there the certificate was intrusted to an agent, with authority from his principal to borrow money upon it for the benefit of his principal, and that he simply exceeded his authority by borrowing more than he was authorized to borrow, and absconding with the excess. (The learned judge proceeded to consider that decision.)

The principles of agency are, however, applicable to this case. In disposing of a pledge, the pledgee acts under a power from the pledgor. The distinction between a lien and a pledge is said to be, that a mere lien cannot be enforced by sale by the act of the party, but that a pledge is a lien with a power of sale superadded. (Story on Bailments, 7th ed., § 311, note 2; Wasson v. Smith, 2 B. & Ald., 439.) The pledgee in selling, is bound to protect the interests of the pledgor, and as to the surplus, represents the pledgor exclusively. Now, for what purpose was the apparent ownership and power of disposition of this stock vested in the brokers? Surely for the purpose of enabling them, effectually and summarily, to execute this power under certain conditions. If the power was absolute on its face, or if the whole legal title was by the instrument apparently vested in the pledgee, and the condition was secret, wherein does the case differ in principle from one of ordinary agency.

I am at a loss to conceive on what principle it can be claimed, that an apparent naked authority is more effectual to bind the party giving it, than an apparent ownership as well as authority. (The learned judge next reviewed various authorities.)

* * * * *

My conclusion is, that the Tenth National Bank must, on the facts found, be deemed to have advanced *bona fide* on the credit of the shares, and of the assignment and power executed by the plaintiff, and is entitled to hold the stock for the full amount so advanced, and remaining unpaid after exhausting the other securities received for the same advance.

The judgment of the General Term, should be modified, so as to allow the plaintiff to redeem, on payment of the balance due to the

Tenth National Bank, on its advance of June 19th, 1868, and the costs of the action.

All concur, except ALLEN and FOLGER, JJ., not voting.

*Judgment modified.*¹⁷

SCOLLANS v. ROLLINS.

1901. 179 Mass. 346, 60 N. E. 983, 88 Am. St. 386.¹⁸

TWO ACTIONS OF TORT originally brought in the Municipal Court of Boston, each for the alleged conversion of a registered certificate of said city for the sum of \$1,000 with an assignment on the back signed in blank by one William Scollans, the defendant, E. H. Rollins & Sons, being a corporation. The jury found for the plaintiff in both cases; and the defendant alleged exceptions.

HOLMES, C. J., These are actions for the conversion of two certificates of indebtedness of the city of Boston, payable to William Scollans, and transferable only at the office of the city treasurer. On the back of each was an assignment in blank, executed and acknowledged by William Scollans, (see Pub. Sts. c. 77, § 6,) by virtue of which, coupled with a delivery of the instruments, the plaintiff became the owner. On the most favorable evidence for the plaintiff, as we must take the case, the plaintiff went to one Gage of the firm of Gage and Felton, bankers and brokers, and said that he would like to leave the certificates in the firm's safe-keeping. Gage consented and asked for the certificates, and the plaintiff handed them to him. Gage went into the next room where the safe was, and returned in a short time with a large envelope, upon which was written the plaintiff's name and the words "Private Property." Gage then put the certificates into the envelope, sealed it, and carried it into the safe. Later the certificates were pledged by Gage and Felton for their debt, and were sold at auction in due course by the pledgee, and bought in the usual course and in good faith by the defendant. The case already has been before the court. 173 Mass.

¹⁷ Cf. *Merchants' Bank v. Livingston* (1878) 74 N. Y. 223, distinguishing the principal case.

¹⁸ See *Merchants' Bank v. Weill* (1900) 163 N. Y. 486, 57 N. E. 749, 79 Am. St. 605; *Elyea v. Lehigh Salt Mining Co.* (1901) 169 N. Y. 29, 61 N. E. 992; *In re Mills* (1908) 125 App. Div. (N. Y.) 730, 110 N. Y. S. 314; (affd. 193 N. Y. 626); *In re Pennsylvania R. Co.'s Appeal* (1878) 86 Pa. St. 80; *Colonial Bank v. Cady & Williams* (1890) L. R. 15 App. Cas. 267; also note, 25 Harv. Law Rev. 74.

In *Central Trust Co. v. West India Improvement Co.* (1901) 169 N. Y. 314, 62 N. E. 387, Cullen, J. said (pp. 328-9): "Certificates of stock are neither choses in action nor negotiable instruments; but both in England and in this country it has been sought to render dealings in stocks practicable and to secure the rights of purchasers by giving to stock certificates attributes of negotiability to a certain limited extent."—Eds.

¹⁹ Statement abridged.—Eds.

275. The difference between its present aspect and that upon which the court has passed is that at this trial evidence was offered, in accordance with an intimation in 173 Mass. 279, of the usage of those engaged in the business of buying and selling such securities, which was intended to show that by their general understanding and practice such an indorsement in blank enabled the bearer to give a good title to a bona fide purchaser. The court ruled, however, that the only question for the jury to consider was another issue, which now is immaterial, as the jury found for the plaintiff upon it, and the defendant excepted.

A blank indorsement of such an instrument signifies that some person is expected to have the right to fill in the blank. On its face it does not indicate who that person is. By itself it is ambiguous. If, however, the general understanding of all concerned gives it a certain meaning, then it has that meaning by the same convention that gives a certain meaning to spoken or written words. The combination of words and blank is a sign as truly as a completed sentence,—a sign which conveys an idea as definitely as if the word “bearer” had been written in. The extent to which the owner shall be estopped by permitting the sign to remain upon the instrument in that form may be enlarged or limited by considerations of policy more or less articulate. No doubt, if such an instrument were stolen from the owner and indorser before his indorsement had become effective by a transfer or before the instrument had been put into other hands, even a bona fide purchaser would not get a title, and a different rule would be applied from that which is established in the interest of the currency with regard to bank notes used as money, and which might be extended to other bills and notes which are negotiable in the true sense. Knox v. Eden Musee American Co. 148 N. Y. 441. 1 Morawetz, Corp. (2d ed.) § 190. See Wyer v. Dorchester & Milton Bank, 11 Cush. 51; Worcester County Bank v. Dorchester & Milton Bank, 10 Cush. 488; Wheeler v. Guild, 20 Pick. 545, 553; Spooner v. Holmes, 102 Mass. 503, 508. But if the owner of the instrument intrusts it to another, he does so charged with notice of the power to deceive which he is putting into that other's hands, and if deception follows he must bear the burden. Colonial Bank v. Cady, 15 App. Cas. 267, 278, 285, 286. Jarvis v. Rogers, 13 Mass. 105; s. c. 15 Mass. 389. McNeil v. Tenth National Bank, 46 N. Y. 325. Burton's Appeal, 93 Penn. St. 214. Pennsylvania Railroad's Appeal, 86 Penn. St. 80. Mount Holly, Lumberton, & Medford Turnpike Co. v. Ferree, 2 C. E. Green, 117. National Safe Deposit, Savings & Trust Co. v. Gray, 12 App. D. C. 276, 287. 1 Morawetz, Corp. (2d ed.) §§ 185-192. See White v. Duggan, 140 Mass. 18, 20; Union Credit Bank v. Mersey Docks & Harbour Board, [1899] 2 Q. B. 205; Pence v. Arbuckle, 22 Minn. 417. In this case, as in some others, it cannot be said that the owner is free from all obligation to contemplate the possibility of wrong-

Dele.

Paulo

doing by a third person. See *Glynn v. Central Railroad*, 175 Mass. 510, 511.

There is nothing in the judgment delivered in *Shaw v. Spencer*, 100 Mass. 382, contrary to what we have said. The customary understanding as to the significance of an indorsement in blank could not relieve the taker from notice of a trust expressed on the face of the document, and of the consequence that the trustee had no power to pledge the instrument for his private debt. So very possibly in the case of an indorsement by the executor of a registered holder. *Colonial Bank v. Cady*, 15 App. Cas. 267. But see *Wood's Appeal*, 92 Penn. St. 379. Or by a guardian. *O'Herrin v. Gray*, 168 Mass. 573. Perhaps it may be as well to add that the usage supposed does not create a new class of negotiable instruments or attempt to enlarge the city of Boston's promise, as was attempted in *Partridge v. Bank of England*, 9 Q. B. 396. It simply fixes the meaning of an ambiguous expression, for the purpose of determining whether it is open to the former owner to deny that the property in the paper and the equitable benefit of the promise have passed to another.

It follows from what we have said that if there was evidence in this case that the plaintiff intrusted the instruments to Gage, and if there was evidence from which the jury would have been warranted in finding the supposed usage proved, the case should have been left to them upon those issues also, and the defendant's exceptions must be sustained.

There was evidence of the alleged usage. Witnesses testified that certificates indorsed as these were, "would be regarded as bearer's certificates passing by delivery from hand to hand"; that they "would be regarded as bearer's property the same as a coupon bond", that they "were considered negotiable." It is true that on cross-examination the witnesses admitted that if an unknown person came in with such instruments for sale they should take some measures to find out that they were dealing with a responsible man, but, apart from the fact that it always is for the jury to decide how far an absolute statement on direct examination shall be cut down by any qualification or contradiction elicited by the other side, *Purple v. Greenfield*, 138 Mass. 1, 7, the jury would have been warranted in regarding these admissions as simply expressing the natural caution of respectable business men who wished to avoid the possibility of question or of having anything to do with a questionable affair. See *Danvers Bank v. Salem Bank*, 151 Mass. 280, 284; *Hinckley v. Union Pacific Railroad*, 129 Mass. 52, 58, citing *Miller v. Race*, 1 Burr. 452; also 2 *Thomp. Corp.* § 2589.

But my brethren are of opinion that there was no evidence that the instruments were intrusted to Gage. It may be assumed that a delivery of possession for custody is a sufficient intrusting. See *Hatfield v. Phillips*, 12 Cl. & Fin. 343, 360; s. c. 14 M. & W. 665, 670. On the other hand if the certificates had been handed to him in a sealed envelope, they would not have been entrusted to him, and

opening the envelope would have been like a carrier's breaking bulk. The modern decisions have followed the ancient suggestion that in such cases there is no delivery of the contents of the enclosure. Choke in Y. B. 13 Ed. IV. 9, pl. 5. 3 Inst. 107. 1 Hale P. C. 504, 505. Belknap v. National Bank of North America, 100 Mass. 376, 381. My brethren consider that the bailment to Gage in the form which it finally took was a bailment of the envelope under seal. In their opinion the transaction cannot be divided, and it does not matter in what form it began. It was not complete until the plaintiff saw the envelope sealed, after having asked Gage to put an insurance policy into the envelope with the bonds, thus showing that he contemplated and assented to the sealing up, which he saw was about to take place. They think it plain that after the plaintiff had seen the envelope sealed and placed in the safe and had departed Gage would not have been at liberty to open the envelope, if, for instance, he found it more convenient for safe-keeping to put the bonds away unenclosed. I have not been able to bring my mind to think that the jury were not at liberty to take a different view, but upon that point I stand alone.

An exception was taken to the admission of the checks made by Gage and Felton payable to the order of Scollans. By way of contradicting the defendant's evidence that the plaintiff's account with Gage and Felton was short and that these instruments were delivered to him as security, the plaintiff testified that he lent them money on one or two occasions, which was repaid by their checks. These checks were dated in August, a month when by the defendant's evidence the plaintiff was heavily indebted to Gage and Felton. They tended as far as they went to corroborate the plaintiff's case, and were admissible as against a merely general objection.

We see no reason for not allowing the ordinary rate of interest after the plaintiff acquired a claim for money against the defendant.

*Exceptions overruled.*¹⁹

RUSSELL v. AMERICAN BELL TEL. CO.

1902. 180 Mass. 467, 62 N. E. 751.

BILL IN EQUITY against the American Bell Telephone Company, a Massachusetts corporation, one Charles M. Gleason, a stock-broker, and the Beacon Trust Company, to enjoin the transfer of eight shares of stock of the defendant telephone company and to require the delivery of the certificate representing those shares to the plaintiff whose testatrix had intrusted them to the defendant Gleason who

¹⁹ See also Shattuck v. American Cement Co. (1903) 205 Pa. 197, 54 Atl. 785, 97 Am. St. 735; Weaver v. Barden (1872) 49 N. Y. 286.—Eds.

fraudulently had pledged them to the defendant trust company to secure his own note, filed March 29, 1900.

In the Superior Court, the case was heard by MASON, C. J., who made a decree for the plaintiff, ordering the defendant trust company to deliver the certificate to the plaintiff by a proper transfer and the defendant telephone company upon surrender of the certificate to issue to the plaintiff a new certificate for the stock represented by the certificate surrendered. From this decree the defendant appealed.

The judge found the facts to be as follows:

The plaintiff is the executrix of the will of Caroline M. Russell, late of Medford, deceased. The plaintiff's testatrix, in April, 1897, was the owner of eight shares of the capital stock of the American Bell Telephone Company, which stood in her name on the books of that company and have not since been transferred thereon. The testatrix was then seventy-five years old or more and was in feeble health, but had full mental capacity to transact business. The defendant Gleason was then a stockbroker doing business in Boston, but living near the testatrix, and had at times advised and assisted her in business transactions and was believed by her to be entirely trustworthy. The defendant telephone company was then about to increase its capital stock, and had issued notice to its stockholders of their right to subscribe for new stock in proportion to their several holdings. The defendant Gleason knew that the testatrix had the eight shares of stock, and, without being requested to do so, called at her house in the evening, when he had reason to believe she was alone, and when she was alone, and informed her of her right to take new stock, advised her to avail herself of that right, and offered his assistance to enable her to surrender her certificate of eight shares and obtain one for the larger number, which should include the new stock. Acting upon the advice and under the direction of Gleason, the testatrix signed the transfer upon the back of the certificate for eight shares, in blank, and, for the purpose of surrendering the certificate to the company and obtaining in place a new certificate which should include the new stock to be taken, and for no other purpose, delivered the certificate to Gleason. Gleason did not seek to obtain a new certificate, but fraudulently pretended to do so, that he might obtain possession of the certificate and use it as security for a loan or loans to himself until he should be able to repay such loan or loans and then deliver the certificate to the company pursuant to the purpose for which it was intrusted to him. Gleason did not surrender the certificate to the company, but converted it to his own use, and fraudulently represented to the defendant trust company, that he was the owner of the stock represented by the certificate, and delivered the certificate to that company in pledge to secure his own note for \$2,500. The defendant trust company took the pledge for value in good faith without knowledge of the fraud of Gleason.

"There is a custom among banks and brokers for certificates like

that in question, with the transfer on the back signed in blank, to pass from hand to hand without inquiry as to the title of the party in possession unless some special cause for suspicion exists, but said Caroline M. Russell did not have knowledge of this custom."

Gleason still owed the defendant trust company \$2,300 on the note, to secure which he fraudulently pledged the certificate, and the trust company still held the certificate.

The plaintiff's testatrix Caroline M. Russell never learned of the fraudulent acts of Gleason, and, a short time after she intrusted the certificate in question to him for surrender to the defendant telephone company, was stricken with paralysis, and until her death, more than two years later, was incapacitated and unable to attend to any business. After her death and the appointment of the plaintiff as executrix under her will, there was no unreasonable delay in ascertaining the facts and taking action to secure the plaintiff's rights.

HOLMES, C. J. The plaintiff's testatrix intrusted a certificate of stock, indorsed in blank, to a fraudulent agent, and he, instead of using it for the purpose for which it was intrusted to him, obtained an advance from the defendant by giving the certificate in pledge. The case, therefore, so far, falls within the general reasoning of *Scollans v. Rollins*, 179 Mass. 346, and the usage referred to in that case was found to be proved.

In order to avoid the intimations of *Scollans v. Rollins*, the plaintiff sets up that in this case only the possession of the certificate, not the property, passed to the agent and that, as the possession was obtained by fraud, it was obtained by larceny in judgment of law. In *Scollans v. Rollins* it is admitted that the general principle there laid down would not apply to an instrument indorsed in blank and stolen before it had been transferred. We shall not examine the premises of this defense because we cannot accept the conclusion. The qualification of the rule, as not applying when the instrument is stolen, is not based upon the name of the agent's crime but upon the fact that in the ordinary and typical case of theft the owner has not intrusted the agent with the document and therefore is not considered to have done enough to be estopped as against a purchaser in good faith. He certainly has not done enough if the estoppel is based upon the principle that when one of two innocent persons is to suffer the sufferer should be the one whose confidence put into the hands of the wrongdoer the means of doing the wrong. But in a case like the present the agent has been intrusted with the converted property, and it is totally immaterial whether, by a stretch which extends larceny beyond the true field of trespass, his wrong has been brought within the criminal law or not. The ground of the estoppel is present and the estoppel arises.

The distinction is not new. On the one side are cases like *Knox v. Eden Musee Americain Co.* 148 N. Y. 441, where an agent or servant simply had access to a document remaining in the possession

of the owner; on the other, cases like Pennsylvania Railroad's Appeal, 86 Penn. St. 80, where possession is intrusted to the agent for one purpose and he uses it for another. It cannot matter in the latter class that the agent intended the fraud from the outset. See further *Brocklesby v. Temperance Permanent Building Society*, [1895] A. C. 173, 181; *Farquharson v. King*, [1901] 2 K. B. 697.

It is found by the court that the testatrix did not know of the custom, and if the question before us were the construction of a contract, her knowledge might be important. But she knew that she was putting into her agent's hands an instrument which made actual deceit possible, and it is not argued for the plaintiff that, under such circumstances and considering the nature of the usage which has been adopted as law in many jurisdictions, she did not take the risk of the appearances being interpreted as it is usual for business men to interpret them.

It may be that the case is sufficiently disposed of by St. 1884, c. 229. It certainly is within the words of that act.

*Decree reversed.*²⁰

²⁰ In *Knox v. Eden Musee Americain Co.* (1896) 148 N. Y. 441, 42 N. E. 988, 31 L. R. A. 779, 51 Am. St. 700, referred to in the principal case, Andrews, Ch. J. said: "The courts have been frequently importuned to extend the qualities of negotiability of stock certificates beyond the limits mentioned, and clothe them with the same character of complete negotiability as attaches to commercial paper, so as to make a transfer to a purchaser in good faith, for value, equivalent to actual title, although there was no agency in the transferrer, and the certificate had been lost without the fault of the true owner or had been obtained by theft or robbery. But the courts have refused to accede to this view, and we have found no case entitled to be regarded as authority which denies to the owner of a stock certificate which has been lost without his negligence, or stolen, the right to reclaim it from the hands of any person in whose possession it subsequently comes, although the holder may have taken it in good faith and for value. The precise question has not often been presented to the courts, for the reason probably that they have with great uniformity held that stock certificates were not negotiable instruments in the broad meaning of that phrase, but, whenever the question has arisen, it has been held that the title of the true owner of a lost or stolen certificate may be asserted against any one subsequently obtaining its possession, although the holder may be a bona fide purchaser. (*Anderson v. Nicholas*, 28 N. Y. 600; *Bangor Electric Light & Power Co. v. Robinson*, 52 Fed. Rep. 520; *Biddle v. Bayard*, 14 Pa. St. 150; *Barstow v. Savage Mining Co.*, 64 Cal. 388. See *Shaw v. R. R. Co.*, 101 U. S. 557.) It may be observed that the elaborate opinion of Judge Rapallo in *McNeil v. Tenth National Bank*, to show that the plaintiff in that case was estopped from asserting his title on the ground of implied agency, was quite unnecessary if a transfer of a stock certificate indorsed in blank to a *bona fide* holder conferred a title as against the true owner, irrespective of the fact whether he voluntarily parted with the possession or was deprived of it by felony or fraud. It is plain, we think, that the argument in support of the judgment in this case, based on the complete negotiability of stock certificates, is not supported by, but is contrary to the decisions. If public policy requires that a further advance should be made in more completely assimilating them to commercial paper in the qualities of negotiability, the legislature and not the courts should so declare. * * * The surrendered certificates were placed by the company in its safe in its office, of which Jurgens had the key, and thereby, it may be said, afforded him the opportunity to commit the crime of which he was guilty, in

IN RE BAHIA & SAN FRANCISCO R. CO., LIM.

1868. L. R. 3 Q. B. Cas. 584.²¹

On March 8th 1866, Miss Trittin was the registered holder of five shares in the Bahia and San Francisco Railway Co., Limited, and deposited the certificates with Oldham, a stock-broker requesting him to keep same and receive the dividends. On or about April 17th 1866, a transfer of the five shares to Stocken and Goldner, purporting to be executed by Miss Trittin, but which is admitted to have been a forgery, was left with the secretary of the company for registration, together with the certificates of the shares. The secretary, in the ordinary course of business, wrote to Miss Trittin, notifying her that the transfer had been so left, and receiving no answer after ten days, registered the transfer and removed the name of Miss Trittin from, and placed the names of Stocken and Goldner upon, the register as holders of the five shares, and certificates for said shares were given to them. Subsequently, Stocken and Goldner sold the five shares to a stockbroker, one Bristowe, who in turn transferred four of the shares to Mr. Burton, and the remaining one to Mrs. Goodburn, bona fide purchasers for value without notice. On or shortly after May 28th 1866, said purchasers were duly registered by the company as the holders of the shares, and certificates were handed to them. It was afterwards discovered the transfer to Stocken and Goldner was a forgery, and on May 11th, 1867 the company was ordered by rule of court to restore the name of Miss Trittin to the register.

The questions herein were:—1. Whether, as against the company, Mr. Burton and Mrs. Goodburn are entitled to said shares or an equivalent number. 2. Whether they are entitled to any and what damages to be paid to them by the company.

COCKBURN, C. J. I am of opinion that our judgment must be for the claimants. If the facts are rightly understood, the case falls within the principle of *Pickard v. Sears*, 6 Ad. & E. 469, and *Free-*

abstracting and uttering them as valid. But it is not true as a general rule that a man may not intrust his property to the custody of his servant, except at the peril of losing his title thereto if the servant steals and disposes of it to another. There must be something more than the mere intrusting to a servant of the custody of a chattel and the consequence opportunity for theft, in order to preclude the master from reclaiming it, if stolen by the servant and sold to another." (pp. 456-8.) The learned court *held*, accordingly, that the company's acts were not such negligence as to estop it from claiming the certificates from a *bona fide* holder thereof to whom Jurgens had fraudulently delivered them.

See also *Jennie Clarkson Home v. Missouri K. & T. R. Co.* (1905) 182 N. Y. 47, 74 N. E. 571, 70 L. R. A. 787; *American Exchange Nat. Bank v. Woodlawn Cemetery* (1909) 194 N. Y. 116, 87 N. E. 107; *Hall v. Wagner* (1906) 111 App. Div. (N. Y.) 70, 97 N. Y. S. 570; *Matter of Mills* (1908) 125 App. Div. (N. Y.) 730, 110 N. Y. S. 314, affirmed 193 N. Y. 626.—Eds.

²¹ Statement abridged. Concurring opinions of Blackburn and Lush, JJ. omitted.—Eds.

man v. Cooke, 2 Ex. 654; 18 L. J. Ex. 114. The company are bound to keep a register of shareholders, and have power to issue certificates certifying that each individual shareholder named therein is a registered shareholder of the particular shares specified. This power of granting certificates is to give the shareholders the opportunity of more easily dealing with their shares in the market, and to afford facilities to them of selling their shares by at once showing a marketable title, and the effect of this facility is to make the shares of greater value. The power of giving certificates is, therefore, for the benefit of the company in general; and it is a declaration by the company to all the world that the person in whose name the certificate is made out, and to whom it is given, is a shareholder in the company, and it is given by the company with the intention that it shall be so used by the person to whom it is given, and acted upon in the sale and transfer of shares. It is stated in this case that the claimants acted bona fide, and did all that is required of purchasers of shares; they paid the value of the shares in money on having a transfer of the shares executed to them, and on the production of the certificates which were handed to them. It turned out that the transferors had in fact no shares, and that the company ought not to have registered them as shareholders or given them certificates, the transfer to them being a forgery. That brings the case within the principle of the decision in *Pickard v. Sears*, 6 Ad. & E. 469, as explained by the case of *Freeman v. Cooke*, 2 Ex. 654, 18 L. J. Ex. 114, that, if you make a representation with the intention that it shall be acted upon by another, and he does so, you are estopped from denying the truth of what you represent to be the fact.

The only remaining question is, what is the redress to which the claimants are entitled. In whatever form of action they might shape their claim, and there can be no doubt that an action is maintainable, the measure of damages would be the same. They are entitled to be placed in the same position as if the shares, which they purchased owing to the company's representation, had in fact been good shares, and had been transferred to them, and the company had refused to put them on the register, and the measure of damages would be the market price of the shares at that time; if no market price at that time, then a jury would have to say what was a reasonable compensation for the loss of the shares.

MELLOR, J. I am of the same opinion. I think the right of action cannot be grounded on negligence; but that the facts do amount to an estoppel on the company from denying the claimant's title. The company need not register a person as a member, under a transfer of shares of which they have any doubt; but can leave the transferee to come to the Court and make out his title. In the present case the company acted apparently without negligence, on the production of the transfer by the broker, and having sent a letter to Miss Trittin and received no answer, they caused the transferees to be registered, and gave them a certificate under seal, clearly intend-

ing them to use it in the market as a voucher or statement that they were the holders of the particular shares. The claimants accordingly purchase the shares, but it turns out that they acquired no title, and their names are struck off the register. I cannot but think that a person must have a remedy against a company for wrongfully striking his name off the register, so as to prevent his having the advantage of the shares he had purchased, and in such an action by the claimants the estoppel would arise against the company. The measure of damages would be the value of the shares at the time they ceased to be recognized as shareholders. Whether or not the company may have a remedy over against Stocken and Goldner it is unnecessary to consider.

PER CURIAM. The rule will be that the company do pay to the claimants the value of their respective shares on the 10th of October, 1866, at interest from that time at 4 per cent., as damages, together with costs.

*Rule absolute accordingly.*²²

SHEFFIELD CORPORATION v. BARCLAY.

1905. L. R. (1905) A. C. 392.²³

ACTION brought by the corporation of Sheffield against Messrs. Barclay & Co., bankers, to recover the sum of 11,487l. 17 s. 5d., being the amount of principal and interest of certain corporation stock which belonged to certain trustees named Timbrell and Honnywill, and was transferred to a nominee of the defendants under a transfer purporting to be executed by Honnywill, but which, for the purpose of this action, must be taken to have been a forgery.

Prior to April 13, 1893, 8500l. Sheffield Corporation Redeemable Stock was transferred to the names of A. A. Timbrell and A. O. Honnywill, who were trustees of a certain estate. The certificate of stock in their names bearing date April 13, 1893, was produced at the trial. The stock had stood in the name of Sutcliffe from 1886, but had been transferred, on change of trustees to Timbrell and Honnywill on March 29, 1893, and on April 13, 1893, a certificate was issued in their names. Upon April 11, 1893, a transfer of 8200l. of this stock to E. E. Barclay, a representative of the defendants, purporting to be executed by Timbrell and Honnywill, was handed to the defendants Barclay & Co. The signature of Honnywill to the transfer of April 11 was a forgery. On April 15, 1893, the defendants Messrs. Barclay & Co. sent the transfer of the 11th to the corporation, inclosed in a letter in the following terms: "54, Lombard

²² Cf. *First Ave. Land Co. v. Parker* (1901) 111 Wis. 1, 86 N. W. 604, 87 Am. St. 841.—Eds.

²³ Statement abridged from the report in the Court of Appeal, (1903) 2 K. B. 580. Concurring opinions omitted.—Eds.

Street, London, E. C., April 15, 1893. Messrs. Barclay, Bevan, Ransom & Co. present their compliments to the registrar of the Sheffield Corporation, and beg to send inclosed the transfer of 8200l. 3½ per cent. 1883 stock, and will be obliged by his registering the same in the company's books in the name of their Mr. E. E. Barclay, sending them the new certificates in due course. Messrs. Barclay & Co. also inclose the amount of the registration fee. The Registrar, Sheffield." This was followed by a letter of the 17th from the registrar, acknowledging the receipt, but pointing out that the registration fee had not been sent; and on April 18, Messrs. Barclay & Co. sent the registration fee. On April 28, 1893, E. E. Barclay, the transferee named in the forged transfer of April 11, executed a transfer of 8000l. of the stock to Messrs. Young and Macdonald, and, upon May 12, of the balance, 200l., to Mary Florence Cockayne. Upon June 1 the plaintiffs issued certificates to Young & Macdonald for the 8000l. and to Mary Cockayne for the 200l. In the year 1901 an action was brought by Honnywill against the corporation, claiming the rectification of the register by inserting his name as the holder of the 8200l. stock transferred to E. E. Barclay under the forged transfer and the interest and dividends paid thereon. In that action the jury found that the transfer was a forgery and had not been executed by Honnywill or with his authority, and for the purpose of this action it was agreed that the defendants were bound by that finding. The corporation was compelled to buy equivalent stock, correctly register it, and pay dividends and interest.

The learned trial judge found as a fact that there was no negligence either on the part of the defendants or their agents, or on the part of the registrar or of any official of the corporation. And came to the conclusion that, as between the two innocent persons, the plaintiffs and the defendants, the loss should be borne by the defendants, who had innocently caused the plaintiffs to act upon an instrument which turned out to be invalid. And he gave judgment for the plaintiffs for the amount claimed, and made a declaration that the plaintiffs were entitled to be indemnified by the defendants in respect of the liabilities arising out of the transactions. See opinion of Lord Alverstone, C. J., (1903) 1 K. B. 1.

The defendants appealed to the Court of Appeal, which reversed the decision below. See *Corporation of Sheffield v. Barclay*, (1903) 2 K. B. 580.

Appeal was then taken by the plaintiffs to the House of Lords. The House took time for consideration.

LORD DAVEY. My Lords, the appellants are suing the respondents upon an implied contract to indemnify them against the liability which has been incurred by them in these circumstances. On April 11, 1893, the respondents, Barclay & Co., Limited, forwarded to the appellants a transfer of Sheffield Corporation Stock purporting to be executed by two persons named Timbrell and Honnywill, who were the registered holders of the stock, in favour of the respondent

Barclay, with a request to the appellants to register the name of the last-named respondent and forward certificates in due course. The appellants acted upon this request, and granted a new certificate to the respondent Barclay, who afterwards transferred the stock for value to third parties. The names of Barclay's transferees were registered in due course, and it is admitted that they obtained a good title against the appellants. All parties believed that the signatures to the transfer from Timbrell and Honnywill were genuine, but, in fact, Honnywill's signature had been forged by Timbrell. It was not, however, until 1899, after Timbrell's death, that Honnywill discovered the fraud; and he thereupon brought an action against the present appellants for rectification of the register and other relief, and recovered judgment against the appellants under which they have incurred a large liability.

On these facts Lord Alverstone C. J., who tried the action, has held that the appellants are entitled to be indemnified by the respondents against the liability they have incurred; but his judgment has been reversed by the Court of Appeal, Vaughan Williams, Romer, and Stirling L. JJ. Before referring to the numerous authorities which have been cited, I will first state the grounds upon which I have come to the conclusion that the Lord Chief Justice was right and his judgment should be restored.

Not much turns upon the particular provisions in the corporation's private Act of 1883 as to the transfer of their debenture stock, or the keeping of the register, or the issue of certificates of title. They for the most part follow the lines of the similar provisions in the Companies Clauses Act. I think that the appellants have a statutory duty to register all valid transfers, and on the demand of the transferee to issue to him a fresh certificate of title to the stock comprised therein. But, of course, it is a breach of their duty and a wrong to the existing holders of stock for the appellants to remove their names and register the stock in the name of the supposed transferee if the latter has, in fact, no title to require the appellants to do so. I am further of opinion that where a person invested with a statutory or common-law duty of a ministerial character is called upon to exercise that duty on the request, direction, or demand of another (it does not seem to me to matter which word you use), and without any default on his own part acts in a manner which is apparently legal but is, in fact, illegal and a breach of the duty, and thereby incurs liability to third parties, there is implied by law a contract by the person making the request to keep indemnified the person having the duty against any liability which may result from such exercise of the supposed duty. And it makes no difference that the person making the request is not aware of the invalidity in his title to make the request, or could not with reasonable diligence have discovered it.

I think that this is the broad principle to be deduced from such cases as *Humphrys v. Pratt*, 5 Bli. (N. S.) 154, 35 R. R. 41; *Betts*

v. Gibbins, 2 Ad. & E. 57, 41 R. R. 381; Toplis v. Grane, 5 Bing. (N. C.) 636, 50 R. R. 814 and the other cases which have been cited. In *Humphrys v. Pratt*, 5 Bli. (N. S.) 154, 35 R. R. 41, the reasons for the judgment in this House are unfortunately not stated in the report; but in commenting on that case in *Collins v. Evans*, 5 Q. B. 804, at p. 829, 64 R. R. 647, Tindal C. J. says: "The declaration states that the judgment creditor pointed out the goods and required the sheriff to take them. He made the sheriff his mandatory or agent for the purpose of taking the goods, and if the sheriff, acting innocently in obedience to that command, commits a trespass, there is no doubt, but he, as any other individual in that position, whether sheriff or not, may recover over against his master or principal the damages he has been obliged to pay in consequence of obeying such directions." In *Toplis v. Grane*, supra, the same judge, after referring to the evidence in the case says: "We think this evidence brings the case before us within the principle laid down by the Court of Queen's Bench in *Betts v. Gibbins*, supra, that where an act has been done by the plaintiff under the express directions of the defendant which occasions an injury to third parties, yet, if such act is not apparently illegal in itself but is done honestly and bona fide in compliance with the defendant's directions, he shall be bound to indemnify the plaintiff against the consequences thereof." In *Collins v. Evans*, supra, on the other hand, the sheriff was intrusted with the execution of a writ of ca. sa. against one John Wright, and the defendant pointed out to him a person of the same name as the person liable, and the sheriff acted on the representation and incurred liability. It was held that the defendant was not liable to indemnify the sheriff because he had merely made an innocent representation to the sheriff but he had not required the sheriff to act upon such representation, and had left him to his own discretion whether he would act upon it or not.

It has been said that the principle of these decisions only applies to cases between principal and agent, and employer and employé, and the language of Tindal C. J. in his comment on *Humphrys v. Pratt*, supra, has been thought to give some colour to that suggestion. I am not, however, of that opinion, and the contrary was decided in *Dugdale v. Lovering*, L. R. 10 C. P. 196. It may be that the language of Tindal C. J. was not so felicitous as it usually was; but his meaning is plain that the liability to indemnify the sheriff arose from his having acted in supposed execution of his duty at the request and by the direction of the creditor. In some cases it is a question of fact whether the circumstances are such as to raise the implication of a contract for indemnity; but in cases like the one now before your Lordships, when a person is requested to exercise a statutory duty for the benefit of the person making the request, I think that the contract ought to be implied. It matters not to the corporation whether A. or B. is the holder of stock, but to the purchaser who has paid his purchase-money or the banker who has lent

money on the security of the stock it is of vital interest. The Court of Appeal distinguished the sheriff's cases on the ground that the request was to execute his duty in a particular manner. In the cases in question that was so. But I think the argument hæret in cortice, and is neither logical nor maintainable. It is difficult to imagine a case where a person should innocently request the sheriff to execute a writ which, though apparently regular, is in fact fictitious or invalid. If such a case be possible, it would come within the exact words of *Tindal C. J.*; and I entertain no doubt that the person presenting the writ would be held liable to indemnify the sheriff. It does not seem to matter at what stage of the transaction the request to do an act which turns out to be outside the officer's duty is made. In the present case, as pointed out by Mr. Bankes, the appellants ran no real risk until they issued the new certificate on the demand of the respondents.

The judgment of the learned judges in the Court of Appeal seems to be based mainly on three grounds—(1.) the decision of Lord Lindley (then Lindley J.) in *Anglo-American Telegraph Co. v. Spurling*, 5 Q. B. D. 188; (2.) that there was no consideration for the alleged contract of indemnity; (3.) that the contract, if any, to be implied from the circumstances was a warranty of their title by the transferees, and not a contract of indemnity.

The cases of *Simm v. Anglo-American Telegraph Co.*, 5 Q. B. D. 188 and the *Anglo-American Telegraph Co. v. Spurling*, *supra*, were an action and cross-action which arose out of a forged transfer of some of the company's stock, and were heard together.

The first action was by the persons claiming under the forged transfer against the company for damages for wrongful removal of their names from the register on discovery of the fraud; and the cross-action was by the company against the persons who had brought in the forged transfer for registration for an indemnity. The learned judge decided the first action in favour of the plaintiffs. He also decided the cross-action against the company. With regard to the transferor, he said: "Supposing that he knows nothing wrong about it, are the company entitled to say to him, 'We assume from the fact that you bring this transfer to us that it is a genuine document'? I apprehend that they are not entitled to say so to him. They are only entitled to say to him, 'We assume that you come honestly to us and that you do not know that anything is amiss with regard to the transaction.'" The learned judge then stated his views as to the duties of the company as follows: "It appears to me that a duty is thrown on the company to look to their own register which involves of course the looking after the transfer of stock or shares standing in the names of persons on the register, and that duty the company owe to those who come with transfers, and I do not see any corresponding or conflicting duty on the part of the person who brings the transfer, except, of course that of bringing what he believes to be an honest document. I think the true view

is this, that there being no negligence in the sense of want of care on either side, but there being a duty on the part of the company to keep the register correct and themselves to look after the transfers between innocent parties, the loss must fall on the company." There was an appeal in both cases, and the decision in the first action was reversed, but counsel for the telegraph company did not proceed with the appeal in the cross-action, because, if they succeeded in the first appeal, the telegraph company had not suffered any damage.

My Lords, I am of opinion that the case of *Anglo-American Telegraph Co. v. Spurling*, 5 Q. B. D. 188; and see per Bramwell L. J., p. 205, was also wrongly decided by Lindley J., and I respectfully dissent from both the propositions laid down by him and adopted by the Court of Appeal in the present case. I dissent from the proposition that a person who brings a transfer to the registering authority and requests him to register it makes no representation that it is a genuine document, and I am disposed to think (though it is not necessary to decide it in the present case) that he not only affirms it is genuine, but warrants that it is so. I think that this is the result of the decision in *Oliver v. Bank of England*, [1902] 1 Ch. 610, affirmed in this House under the name of *Starkey v. Bank of England*, [1903] A. C. 114. It may be argued with some force that for this purpose no solid distinction can be made between the power of attorney through which the transfer of Consols is effected and the deed of transfer in the present case. Each of these instruments, it may be said, is put forward as evidence of the authority with which the person making the application professes to be clothed to request the removal of the stockholder's name and the substitution of another name in his place. But, however this may be, it is enough for the decision of this appeal to say that the deed of transfer was put forward as a genuine document, and the appellants were invited to act upon it as such.

I am also of opinion that the authority keeping a stock register has no duty of keeping the register correct which they owe to those who come with transfers. Their only duty (if that be the proper expression) is one which they owe to the stockholders who are on the register. This point was decided by all the learned judges who took part in the decision of the first case of *Simm v. Anglo-American Telegraph Co.*, 5 Q. B. D. 188. I will content myself with quoting the language of Cotton L. J., 5 Q. B. D. p. 214; and see per Bramwell L. J. p. 203, and Brett L. J. p. 209: "The duty of the company is not to accept a forged transfer, and no duty to make inquiries exists towards the person bringing the transfer. It is merely an obligation upon the company to take care that they do not get into difficulties in consequence of their accepting a forged transfer, and it may be said to be an obligation towards the stockholder not to take the stock out of his name unless he has executed a transfer; but it is only a duty in this sense, that unless the company act upon

a genuine transfer they may be liable to the real stockholder." True it is that the appellants, following what is now the usual practice, gave notice of the transfer which had been brought in to the persons named as transferors, but they had no duty to do so, and it was done merely for their own protection. Experience in these cases shews, however, that it is a very poor protection.

Stirling L. J. held that the mere performance of a duty imposed by law upon any one holding a definite legal position does not constitute a consideration sufficient to support a promise to him by the person to whom the duty is owed. But with great respect to that very careful judge, he overlooked that this very point was involved in the decision of the case of *Oliver v. Bank of England* [1902] 1 Ch. at pp. 621, 622. Vaughan Williams L. J. quoted and commented upon the passage from the judgment of Willes J. in *Collen v. Wright*, (1857) 8 E. & B. 647, 658, where he says: "The fact of entering into the transaction with the professed agent as such is good consideration for the promise." And it did not occur either to the learned counsel, who argued the case with great pertinacity, or to any of the learned judges in the Court of Appeal or the noble Lords in this House, to question that the acting by the Bank of England on the demand of the supposed attorney was a good consideration for the promise by him to warrant the genuineness of the power which they held to be established.

Lastly, my Lords, it was said by Romer L. J. that this is not an action on a warranty, and that a warranty and a contract of indemnity are distinct, one important difference being the period from which the Statute of Limitations would run. That, of course, is so, and the appellants admit that if they were suing on the warranty their action would be out of time. But I can see no legal reason why, in circumstances like those of the present case, it should not be held, if necessary, that the true contract to be implied from those circumstances is not only a warranty of the title, but also an agreement to keep the person in the position of the appellants indemnified against any loss resulting to them from the transaction. And I think that justice requires we should so hold. I agree with the Lord Chief Justice that, as between these two innocent parties, the loss should be borne by the respondents who caused the appellants to act upon an instrument which turned out to be invalid.

I am therefore of opinion that the appeal should be allowed, and the judgment of the Lord Chief Justice restored with costs here and below.*

* In rendering the judgment in the Court of Appeal, (1903) 2 K. B. 580, reversed in the principal case, Vaughan Williams, L. J. said: "Before dealing more particularly with the terms of the Sheffield Act and the authorities bearing on the circumstances justifying an implication of a contract of indemnity, I wish to say at once that I regard what the defendants did and the act of the corporation thereupon as being aptly described by the words of Bramwell B. in *Hart v. Frontino, etc., Gold Mining Co.*, L. R. 5 Ex. at p. 115: 'I made you a tender of myself as a shareholder, and you accepted me, and I

have acted upon that acceptance.' And I do not think that the defendants in sending in a transfer to the corporation gave any warranty to the corporation, or made any material representation to the company, that the transferor was the registered holder of the stock: see the judgment of Lord Field in *Balkis Consolidated Co. v. Tomkinson* (1893) A. C. at p. 413, where he says that a purchaser sending in a transfer to the corporation makes no representation which might estop him as against the corporation." (p. 587) And again: "The case, as pointed out by Bramwell B. in *Hart v. Frontino*, etc., *Gold Mining Co.*, L. R. 5 Ex. 111, at p. 115, is analogous to that of a bona fide holder of a bill of exchange presenting it for payment to a banker—if the banker pays it he cannot afterwards recover the money from the holder on the ground that the name of the drawer was forged. Lindley J. took the same view in *Simm v. Anglo-American Telegraph Co.*, 5 Q. B. D. 188, at p. 195. In my judgment the provisions of the special Act bring this case within the observations of Blackburn J. in *In re Bahia and San Francisco Ry. Co.*, L. R. 3 Q. B. 584, at p. 595, approved by Lord Herschell in *Balkis Consolidated Co. v. Tomkinson*, (1893) A. C. at 403. Those observations of Blackburn J. run thus: That when joint stock companies were established the great object was that the shares should be capable of being easily transferred; that the Legislature had accordingly provided for the keeping of a register of the members, in order to keep which the company must alter the register whenever there was a transfer of its shares; and the learned judge drew attention to s. 31 of the Companies Act, 1862, which provides that a company may give certificates, and that these shall be prima facie evidence of the title of the person named to the shares specified, and pointed out that by granting the certificate the company make a statement that they have transferred the shares specified to the person named in it and that he is the holder of the shares; that if the company have been deceived and the statement is not true, they may not be guilty of negligence, but they and no one else had power to inquire into the matter." (pp. 590-1.)

See articles by J. L. Thorndyke, 17 *Harv. Law Rev.* 373, and J. B. Ames, 17 *id.* 543, also note, 16 *id.* 228, discussing the principal case.

Cf. *Boston & Albany R. Co. v. Richardson* (1883) 135 *Mass.* 473; *Oliver v. Bank of England*, (1902) 1 *Ch. Div.* 610, s. c. on appeal, *Starkey v. Bank of England*, (1903) A. C. 114. See also *Leurey v. Bank of Baton Rouge* (1912) 131 *La.* —; 58 *So.* 1022.—Eds.

CHAPTER IX.

CREDITORS.

Section 1.—Relation Between Creditor and Corporation. The Trust Fund Theory.

SAWYER v. HOAG.

1873. 17 Wall. (U. S.) 610, 21 L. Ed. 731.¹

APPEAL from the Circuit Court for the Northern District of Illinois.

About the 1st of April, 1865, and prior, therefore to the passage of the Bankrupt Act of 1867, the directors of the Lumberman's Insurance Company of Chicago—a company then recently incorporated and authorized to begin business on a capital of \$100,000, of which not less than one-tenth should be paid in, the residue to be secured—invited subscriptions to the capital stock of the company; stating, in most instances, to those whom they invited to subscribe, that only 15 per cent. would be required to be paid down in cash, and that the remaining 85 per cent. would be lent back to the subscriber, and a note taken therefor, payable in five years, with 7 per cent. interest, payable semi-annually, secured by collateral security satisfactory to the directors of the company.

In this state of things one Sawyer, about the said 1st of April, 1865, at the solicitation of one of the directors, subscribed for fifty shares of stock. When called upon to close his subscription, he was informed, as indeed all the subscribers were, that the matter would be closed on the plan above mentioned.

Sawyer accordingly complied with the requirements, and gave his check to the company for \$5000, the full amount of his stock, and his note payable to it in five years from date, for \$4250, that is to say, for 85 per cent. of the par value of the stock, by way of, and as for a loan thereof from the company.

The original transaction was regarded and treated by the company and by Sawyer as a loan by the company to him, and his stock was treated as fully paid for. At various times after the giving of the original note, the company reported to the authorities of the State of Illinois and of other States that its capital stock was fully paid.

¹ Statement abridged.—Eds.

On the 8th and 9th day of October, A. D. 1871, a great fire devastated the city of Chicago and rendered the Lumberman's Insurance Company insolvent; and on the 25th of January, 1872—it being at that time a notorious fact, one well understood by the public, and one which Sawyer had good reason to believe, that the said company was insolvent and unable to pay its liabilities—Sawyer purchased of a certain Hayes a certificate of an adjusted loss for \$5,000 against the company for 33 per cent. of its par value.

In June, 1872, after Sawyer had purchased this certificate of adjusted loss, a petition in bankruptcy was filed against the company, and it having been adjudicated a bankrupt, one Hoag was appointed its assignee.

Among the effects of the company, which came into Hoag's hands as assignee, was the already-mentioned note of Sawyer for \$4250, with the securities assigned as collateral. Hoag demanding of Sawyer payment of this note, Sawyer produced his certificate of adjusted loss for \$5000 and insisted on setting it off against the demand, asserting a right to do this under the twentieth section of the Bankrupt Act.

Hoag refused to allow the set-off, and was about to sell the collateral securities in accordance with the power given to him. Hereupon Sawyer filed a bill in the court below to enforce the set-off; in which he alleged, among other things, that the note given by him to the insurance company was for money lent to him.

The assignee, in his answer, denied that the note was for money lent, and averred that it was in fact for a balance due by Sawyer for his stock subscription, which had never been paid, and insisted that such balances constituted a trust fund for the benefit of all creditors of the insolvent corporation, which could not be made the subject of a set-off against an ordinary debt due by the company to one of its creditors. After the general replication, the case was submitted to the court below on an agreed statement of facts. That court decreed against the complainant, and from that decree the case was brought by the present appeal to this court.

MILLER, J.—The first and most important question to be decided in this case is whether the indebtedness of the appellant to the insurance company is to be treated, for the purposes of this suit, as really based on a loan of money by the company to him, or as representing his unpaid stock subscription.

The charter under which the company was organized authorized it to commence business upon a capital stock of \$100,000, with ten thousand paid in, and the remainder secured by notes with mortgages on real estate or otherwise. The transaction by which the appellant professes to have paid up his stock subscription is, shortly, this: He gave to the company his check for the full amount of his subscription, namely, \$5000. He took the check of the company for \$4250, being the amount of his subscription less the 15 per cent. required of each stockholder to be paid in cash, and he gave his

note for the amount of the latter check, with good collateral security for its payment, with interest at 7 per cent. per annum. The appellant and the company, by its officers, agreed to call this latter transaction a loan, and the check of the appellant payment in full of his stock; and on the books of the company, and in all other respects as between themselves, it was treated as payment of the subscription and a loan of money. It is agreed that at this time the current rate of interest in Chicago was greater than 7 per cent., and it is not stated as a fact whether these checks were ever presented and paid at any bank, or that any money was actually paid or received by either party in the transaction. It must, therefore, be treated as an agreement between the corporation, by its officers, on the one part, and the appellant, as a subscriber to the stock of the company, on the other part, to convert the debt which the latter owed to the company for his stock into a debt for the loan of money, thereby extinguishing the stock debt.

Undoubtedly this transaction, if nothing unfair was intended, was one which the parties could do effectually as far as they alone were concerned. Two private persons could thus change the nature of the indebtedness of one to the other if it was found to be mutually convenient to do so. And in any controversy which might or could grow out of the matter between the insurance company and the appellant we are not prepared to say that the company, as a corporate body, could deny that the stock was paid in full.

And on this consideration one of the main arguments on which the appellant seeks to reverse the decree stands. He assumes that the assignee in bankruptcy is the representative alone of the corporation, and can assert no right which it could not have asserted. The weakness of the argument is in this assumption. The assignee is the representative of the creditors as well as the bankrupt. He is appointed by the creditors. The statute is full of authority to him to sue for and recover property, rights, and credits, where the bankrupt could not have sustained the action, and to set aside as void transactions by which the bankrupt himself would be bound. All this, of course, is in the interest of the creditors of the bankrupt.

Had the creditors of this insolvent corporation any right to look into and assail the transaction by which the appellant claims to have paid his stock subscription?

Though it be a doctrine of modern date, we think it now well established that the capital stock of a corporation, especially its unpaid subscriptions, is a trust fund for the benefit of the general creditors of the corporation. And when we consider the rapid development of corporations as instrumentalities of the commercial and business world in the last few years, with the corresponding necessity of adapting legal principles to the new and varying exigencies of this business, it is no solid objection to such a principle that it is modern, for the occasion for it could not sooner have arisen.

The principle is fully asserted in two recent cases in this court,

namely, *Burke v. Smith*,* and in *New Albany v. Burke*.† Both these cases turned upon the doctrine we have stated, and upon the necessary inference from that doctrine, that the governing officers of a corporation cannot, by agreement or other transaction with the stockholder, release the latter from his obligation to pay, to the prejudice of its creditors, except by fair and honest dealing and for a valuable consideration.

In the latter case, a judgment creditor of an insolvent railroad company, having exhausted his remedy at law, sought to enforce this principle by a bill in chancery against the stockholders. The court, by affirming the right of the corporation to deal with the debt due it for stock as with any other debt, would have ended the case without further inquiry. But asserting, on the contrary, to its full extent, that such stock debts were trust funds in their hands for the benefit of the corporate creditors, and must in all cases be dealt with as trust funds are dealt with, it was found necessary to go into an elaborate inquiry to ascertain whether a violation of the trust had been committed. And though the court find that the transaction by which the stockholders had been released was a fair and valid one, as founded on the conditions of the original subscription, the assertion of the general rule on the subject is none the less authoritative and emphatic.*

In the case before us the assignee of the bankrupt, in the interest of the creditors, has a right to inquire into this conventional payment of his stock by one of the shareholders of the company; and on that inquiry, we are of opinion that, as to these creditors, there was no valid payment of his stock by the appellant. We do not base this upon the ground that no money actually passed between the parties. It would have been just the same if, agreeing beforehand to turn the stock debt into a loan, the appellant had brought the money with him, paid it, taken a receipt for it, and carried it away with him. This would be precisely the equivalent of the exchange of checks between the parties. It is the intent and purpose of the transaction which forbids it to be treated as valid payment. It is the change of the character of the debt from one of a stock subscription unpaid to that of a loan of money. The debt ceases by this operation, if effectual, to be the trust fund to which creditors can look, and becomes ordinary assets, with which the directors may deal as they choose.

And this was precisely what was designed by the parties. It divested the claim against the stockholder of its character of a trust fund, and enabled both him and the directors to deal with it

* 16 Wallace, 390.

† 11 Id. 96.

* See also *Curran v. Arkansas*, 15 Howard (U. S.) 304, 14 L. ed. 705; *Wood v. Dummer*, 3 Mason (U. S.) 305; *Slee v. Bloom*, 19 Johnson (N. Y.) 456, and numerous other cases cited by the counsel for the appellees. (The decision of Story, J. in *Wood v. Dummer*, *supra*, decided in 1835, is the origin of the so-called Trust Fund theory.—Eds.)

freed from that charge. There are three or four of these cases now before us in which precisely the same thing was done by other insurance companies organized in Chicago, and we have no doubt it was done by this company in regard to all their stockholders.

It was, therefore, a regular system of operations to the injury of the creditor, beneficial alone to the stockholder and the corporation.

We do not believe we characterize it too strongly when we say that it was a fraud upon the public who were expected to deal with them.

The result of it was that the capital stock of the company was neither paid up in actual money, nor did it exist in the form of deferred instalments properly secured.

It is said by the appellant's counsel that conceding this, it is still a debt due by him to the corporation at the time that he became the owner of the debt due by the corporation to Hayes, and, therefore, the proper subject of set-off under the twentieth section of the Bankrupt Act. That section is as follows: "In all cases of mutual debts or mutual credits between the parties, the account between them shall be stated, and one debt set off against the other, and the balance only shall be allowed or paid, but no set-off shall be allowed of a claim in its nature not provable against the estate: *Provided*, that no set-off shall be allowed in favor of any debtor to the bankrupt of a claim purchased by or transferred to him after the filing of the petition."

This section was not intended to enlarge the doctrine of set-off, or to enable a party to make a set-off in cases where the principles of legal or equitable set-off did not previously authorize it.

The debts must be mutual; must be in the same right.

The case before us is not of that character. The debt which the appellant owed for his stock was a trust fund devoted to the payment of all the creditors of the company. As soon as the company became insolvent, and this fact became known to the appellant, the right of set-off for an ordinary debt to its full amount ceased. It became a fund belonging equally in equity to all the creditors, and could not be appropriated by the debtor to the exclusive payment of his own claim.

It is unnecessary to go into the inquiry whether this claim was acquired before the commission of an act of bankruptcy by the company, or the effect of the bankruptcy proceeding. The result would be the same if the corporation was in the process of liquidation in the hands of a trustee or under other legal proceedings. It would still remain true that the unpaid stock was a trust fund for all the creditors, which could not be applied exclusively to the payment of one claim, though held by the stockholder who owed that amount on his subscription.

Nor do we think the relation of the appellant in this case to the corporation is without weight in the solution of the question before us. It is very true, that by the power of the legislature there is

created in all acts of incorporation a legal entity which can contract with its shareholders in the ordinary transactions of business as with other persons. It can buy of them, sell to them, make loans to them, and in insurance companies, make contracts of insurance with them, in all of which both parties are bound by the ordinary laws of contract. The stockholder is also relieved from personal liability for the debts of the company. But after all, this artificial body is but the representative of its stockholders, and exists mainly for their benefit, and is governed and controlled by them through the officers whom they elect. And the interest and power of legal control of each shareholder is in exact proportion to the amount of his stock. It is, therefore, but just that when the interest of the public, or of strangers dealing with this corporation is to be affected by any transaction between the stockholders who own the corporation and the corporation itself, such transaction should be subject to a rigid scrutiny, and if found to be infected with anything unfair towards such third person, calculated to injure him, or designed intentionally and inequitably to screen the stockholder from loss at the expense of the general creditor, it should be disregarded or annulled so far as it may inequitably affect him.*

These principles require the affirmation of the decree in the present case, and it is accordingly *Affirmed.*²

Mr. Justice HUNT dissented, holding that the transaction was a loan by the company to the appellant.

BARTLETT v. DREW.

1874. 57 N. Y. 587.³

APPEAL from judgment of the General Term of the Supreme Court in the first judicial department, affirming a judgment in

* *Lawrence v. Nelson*, 21 New York, 158.

² See also *Melvin v. Lamar Ins. Co.* (1875) 80 Ill. 446, 22 Am. Rep. 199; *Patterson v. Lynde* (1884) 112 Ill. 196; *Marion Trust Co. v. Blish* (1908) 170 Ind. 686, 84 N. E. 814, 18 L. R. A. (N. S.) 347n; *Hurd v. N. Y. etc. Laundry Co.* (1901) 167 N. Y. 89, 60 N. E. 327, (conveyance in fraud of creditors); *Hazard v. Wight* (1911) 201 N. Y. 399, 94 N. E. 855; *New Albany v. Burke* (1870) 11 Wall. (U. S.) 96, 20 L. ed. 155; *Scovill v. Thayer* (1881) 105 U. S. 143, at p. 152, 26 L. ed. 968.

Cf. O'Bear Jewelry Co. v. Volfer (1894) 106 Ala. 205, 17 So. 525, 28 L. R. A. 707, 54 Am. St. 31; *Vaughn v. Alabama Nat. Bank* (1904) 143 Ala. 572, 42 So. 64. ("Only to this extent does the trust fund theory apply, just as it would to an individual under like circumstances."); *Tradesman Pub. Co. v. Car Wheel Co.* (1895) 95 Tenn. 634, 32 S. W. 1097; *Conover v. Hull* (1895) 10 Wash. 673, 39 Pac. 166, 45 Am. St. 810; *Cottrell v. Albany Card and Paper M'fg Co.* (1911) 142 App. Div. (N. Y.) 148, 126 N. Y. S. 1070; *Assets Collecting Co. v. Barnes-King Development Co.* (1912) 198 Fed. 82. See note, 8 Columbia Law Rev. 303.

Washington Savings Bk. v. Butchers' & Drovers' Bk. (1895) 130 Mo. 155, 31 S. W. 761, *contra*.—Eds.

³ Statement abridged.—Eds.

favor of plaintiff entered upon the report of a referee. (Reported below, 4 Lans., 444.)

This was an action in the nature of a creditor's bill brought by plaintiff as judgment creditor of the New Jersey Steam Navigation Company after the return of an execution, *nulla bona*, to reach certain assets of the said company alleged to be in the hands of defendant, Drew.

REYNOLDS, C. It is insisted by the defendant, Drew, that the plaintiff can maintain no action against him alone, but that she must prosecute not only all the stockholders, to the end that each shall contribute his proportion to the payment of her debt, but her suit must be brought on her own behalf and on behalf of all the other creditors of the corporation who may choose to come in. In other words, in order to collect her debt against the company, she must institute a suit to wind up and finally settle all its affairs. That she *might* do this is not to be doubted, but that she of necessity *must* do it presents a different question. Prior to the distribution of the assets of the corporation, due notice of the plaintiff's claim was given, and redress demanded, and the distribution was made with knowledge of the plaintiff's claim, and the corporation has no assets or property which can be taken on execution.

We are of the opinion that the plaintiff's right of action rests upon a very plain principle of equity. This is not a proceeding to dissolve and wind up the affairs of a corporation, or to marshal its assets, but the ordinary proceeding to collect a debt from a debtor unwilling to pay. The circumstance that the debtor is a foreign corporation, or that the defendant, Drew, was its president, director or stockholder, is quite immaterial, if it be found that Drew has any of the assets or property of the corporation which ought to be applied in payment of its debts. It is equally immaterial, whether he got it by fair agreement with his associates, or by any wrongful act. If the law dooms it to the payment of the debts of the corporation, it may be taken in some form by the creditor. It is a very plain proposition that the stock and property of every corporation is to be regarded as a trust fund for the payment of its debts, and its creditors have a lien and the right to priority of payment over any stockholder. (2 Story Eq. Jur., § 1252.) Where stock and property has been divided between stockholders before all the debts of the corporation have been discharged, if any one stockholder is compelled to pay more than his fair share of any unpaid debt he may resort to his associates for equitable contribution; but with that proceeding the creditor has nothing to do, unless he chooses to intervene to settle equities that may exist between his debtors. In the present case the corporation was proceeded against as an ordinary debtor, either unwilling or unable to pay. It turned out, that it had no property which could be taken on execution; but it was found that the defendant, Drew, had a large amount of the assets in his possession, which belonged to the corporation when the plaintiff's demand

accrued, and some portion of which should have been applied in discharge of its obligation to the plaintiff. As before suggested, it does not matter how it came to the possession of the defendant, Drew. It is enough that he had it, and it was so much of the assets of the corporation as ought to be devoted to the payment of the debts of the company, and his claim as a stockholder could not prevail over the creditor's prior right. (*Curran v. State of Arkansas*, 15 How. [U. S.], 305; *Tinkham v. Borst*, 31 Barb., 407, 412; 2 Kent Com., 307; 2 Story Eq. Jur., § 1252.) This view of the case renders the consideration of several questions argued by the learned counsel for the defendant, Drew, in respect to parties and the form of proceeding, quite unnecessary. We are referred, however, to two cases in Massachusetts, of which a word may be said. (*Vose v. Grant*, 15 Mass., 505; *Spear v. Grant*, 16 id., 9.) They were both actions on the case at common law, by the bill-holder and creditor of a bank, whose charter had expired and assets distributed, against a stockholder who had received a portion thereof. The action proceeded entirely upon the theory that the distribution was wrongful before all the debts of the corporation were paid; and that, for this alleged wrong, an action on the case at common law might be maintained by a creditor against each stockholder who had profited by the wrongful division. After a very elaborate consideration by the court, the right of action was denied, and whether properly or improperly does not affect the present case. The Supreme Judicial Court of Massachusetts had at that time no equity jurisdiction, and this circumstance was lamented by JACKSON, J., in delivering the opinion of the court in the case first cited. Whether the apparent hardship of that case, or possibly of many others, had any influence, it is certain that, soon after, the law-making power of the State conferred upon the court equity jurisdiction. With the nice distinction between law and equity we are not troubled in this case, nor even as to the form of the action. The plaintiff is a creditor of the New Jersey Steam Navigation Company for the amount of a judgment duly obtained. The company has no property in this State that can be taken on execution. The defendant, Drew, is found to be in possession of assets of the dissolved or insolvent corporation more than sufficient to pay the plaintiff her demand, and the law requires that he should pay it.

The judgment below should be affirmed, with costs.

All concur.

Judgment affirmed.

HANDLEY v. STUTZ.

1890. 137 U. S. 366.*

THIS was a bill in equity, filed February 8, 1889, in the Circuit Court of the United States for the Middle District of Tennessee, by citizens of Pennsylvania, of Indiana and of Ohio, judgment creditors of the Clifton Coal Company, in behalf of themselves and all other creditors who should come in and contribute to the expenses of the suit, against that corporation, which was a Kentucky corporation, whose chief officers resided in Tennessee, and against sixteen individuals, alleging that they were stockholders in the corporation and citizens of Tennessee, and had paid nothing for their stock and were liable to the corporation for the amounts thereof, and their liabilities were assets of the corporation and a trust fund for the payment of all its debts; that the corporation was insolvent; and had no other assets that the plaintiffs could reach; and that its officers had declined to collect or to attempt to collect any of the amounts so due to it, and had neglected to administer the trust fund.

MR. JUSTICE GRAY.—This is a bill in equity by some, in behalf of all, of the creditors of a corporation, against the corporation and holders of stock therein. The bill is not founded upon any direct liability of the stockholders to the plaintiffs; but upon the theory that, the corporation being insolvent and having no other assets, the sums due to it from the stockholders on their unpaid subscriptions to stock ought to be paid by them to the corporation as a trust fund to be distributed among the plaintiffs and all other creditors of the corporation, so far as required to satisfy their just claims, and that, the corporation having neglected to collect these sums or to administer the trust, and the plaintiffs and defendants being citizens of different States, the Circuit Court sitting in equity, should compel those sums to be paid in by the stockholders, to be administered as a trust fund and to be distributed among all creditors who should come in. Such a bill can only be maintained by one or more creditors in behalf of all, and not by any one creditor to secure payment of his own debt to the exclusion of others. *Sawyer v. Hoag*, 17 Wall. 610, 622; *Patterson v. Lynde*, 106 U. S. 519; *Johnson v. Waters*, 111 U. S. 640, 674. In *Hatch v. Dana*, 101 U. S. 205, the bill of a single creditor, which was sustained by the court, was brought in behalf of himself and all other creditors of the corporation who should come in and contribute to the expenses of the suit; no other creditors came in; and it did not appear that there were any others. * * *

The trust fund so administered and ordered to be distributed by the Circuit Court amounting to much more than \$5,000, the appellate jurisdiction of this court is not affected by the fact that the amounts

* Portion of statement of facts and opinion omitted.—Eds.

decreed to some of the creditors are less than that sum. It was immaterial to the appellants how the sums decreed to be paid by them should be distributed, and (which is more decisive) such a bill as this could not have been filed by one creditor in his own behalf only, and the case does not fall under that class in which creditors, who might have sued severally, join in one bill for convenience and to save expense. This court, therefore, has jurisdiction of the whole appeal, according to the rule affirmed in *Gibson v. Shufeldt*, 122 U. S. 27, and the cases there collected.

Motion to dismiss appeal overruled, and jurisdiction of the Circuit Court sustained.⁵

HOLLINS v. BRIERFIELD COAL & IRON COMPANY.

1893. 150 U. S. 371, 37 L. ed. 1113, 14 Sup. Ct. 127.*

The Brierfield Coal & Iron Company was incorporated under the laws of Alabama May 4, 1882. On September 1, 1882, a conveyance was made by the company to Preston B. Plumb, as trustee, to secure an issue of \$500,000 in bonds. Subsequently, the trustee, Plumb, filed a bill in the Circuit Court of the United States for the Middle District of Alabama, asking that all creditors of the corporation be permitted to make themselves parties and have their claims adjudicated, that a full administration be had of the estate, and if need be, a foreclosure and sale.

Nearly three months after the commencement of the Plumb suit, and on October 28, 1887, these appellants, as plaintiffs, filed a bill in the same court, making the coal company and sundry stock and bondholders, together with the trustee Plumb, parties defendant. The plaintiffs were unsecured creditors of the company, having claims contracted in 1886 and 1887, four or five years after the issue of the bonds and execution of the trust deed, who sued on behalf of themselves and all other creditors of the coal and iron company, who were willing to come in and contribute to the expenses of the suit. After setting forth their claims, they alleged that the conveyance to Plumb, as trustee, was absolutely void; that a large amount was still due on the stock; they asked to have a receiver appointed, and the property sold in satisfaction of their claims; and that such receiver have authority to collect the unpaid stock subscriptions, to be also applied in satisfaction of their claims. They alleged the pendency of the suit brought by Plumb as trustee, but did not ask to intervene therein. After the decree of foreclosure and sale in the

* See *Harper v. Union Mfg. Co.* (1881) 100 Ill. 225; *Wetherbee v. Baker* (1882) 35 N. J. Eq. 501; *Jauch v. de Socarras* (1898) 56 N. J. Eq. 524, 39 Atl. 381; *Gallagher v. Asphalt Co.* (1903) 65 N. J. Eq. 258, 55 Atl. 259; *Squire v. Princeton Lighting Co.* (1907) 72 N. J. Eq. 883, 68 Atl. 176.—Eds.

⁵ Statement abridged. Portions of opinion omitted.—Eds.

Plumb case, and on July 24, 1889, a final decree was entered dismissing this bill. From such decree of dismissal plaintiffs appealed to this court.

MR. JUSTICE BREWER, after stating the case, delivered the opinion of the court.

The plaintiffs were simple contract creditors of the company; their claims had not been reduced to judgment, and they had no express lien by mortgage, trust deed, or otherwise. It is the settled law of this court that such creditors cannot come into a court of equity to obtain the seizure of the property of their debtor, and its application to the satisfaction of their claims; and this, notwithstanding a statute of the State may authorize such a proceeding in the courts of the State. The line of demarcation between equitable and legal remedies in the Federal courts cannot be obliterated by state legislation. *Scott v. Neely*, 140 U. S. 106; *Cates v. Allen*, 149 U. S. 451. Nor is it otherwise in case the debtor is a corporation, and an unpaid stock subscription is sought to be reached. *National Tube Works Company v. Ballou*, 146 U. S. 517; *Swan Land & Cattle Company v. Frank*, 148 U. S. 603, 612. * * *

But it is earnestly insisted that it has been held by this court, in *Case v. Beauregard*, 101 U. S. 688, that whenever a creditor has a trust in his favor, or a lien upon the property for a debt due him, he may go into equity without exhausting his legal remedies; that it has also frequently been affirmed that the capital stock and assets of a corporation constitute a trust fund for the benefit of its creditors, which neither the officers nor stockholders can divert or waste, and several cases are cited, among them that of *Sanger v. Upton*, 91 U. S. 56, in which perhaps the proposition is asserted in the most direct and emphatic language, and *Terry v. Anderson*, 95 U. S. 628, 636, in which Chief Justice Waite made these observations: "Ordinarily, a creditor must put his demand into judgment against his debtor and exhaust his remedies at law before he can proceed in equity to subject choses in action to its payment. To this rule, however, there are some exceptions; and we are not prepared to say that a creditor of a dissolved corporation may not, under certain circumstances, claim to be exempted from its operation. If he can, however, it is upon the ground that the assets of the corporation constitute a trust fund which will be administered by a court of equity in the absence of a trustee; the principle being that equity will not permit a trust to fail for want of a trustee."

While it is true, language has been frequently used to the effect that the assets of a corporation are a trust fund held by a corporation for the benefit of creditors, this has not been to convey the idea that there is a direct and express trust attached to the property. As said in 2 *Pomeroy's Equity Jurisprudence*, § 1046, they "are not in any true and complete sense trusts, and can only be called so by way of analogy or metaphor."

To the same effect are decisions of this court. The case of

Graham v. Railroad Company, 102 U. S. 148, was an action by a subsequent creditor to subject certain property, alleged to have been wrongfully conveyed by the corporation debtor, to the satisfaction of his judgment. And the very proposition here presented was then considered, and in respect to it, the court, by Mr. Justice Bradley, said (p. 160): "It is contended, however, by the appellant that a corporation debtor does not stand on the same footing as an individual debtor; that, whilst the latter has supreme dominion over his own property, a corporation is a mere trustee, holding its property for the benefit of its stockholders and creditors; and that if it fail to pursue its rights against third persons, whether arising out of fraud or otherwise, it is a breach of trust, and creditors may come into equity to compel an enforcement of the corporate duty. This, as we understand, is the substance of the position taken.

"We do not concur in this view. It is at war with the notions which we derive from the English law with regard to the nature of corporate bodies. A corporation is a distinct entity. Its affairs are necessarily managed by officers and agents, it is true; but, in law, it is as distinct a being as an individual is, and is entitled to hold property (if not contrary to its charter) as absolutely as an individual can hold it. Its estate is the same, its interest is the same, its possession is the same. Its stockholders may call the officers to account, and may prevent any malversation of funds, or fraudulent disposal of property on their part. But that is done in the exercise of their corporate rights, not adverse to the corporate interests, but coincident with them.

"When a corporation becomes insolvent, it is so far civilly dead that its property may be administered as a trust fund for the benefit of its stockholders and creditors. A court of equity, at the instance of the proper parties, will then make those funds trust funds, which, in other circumstances, are as much the absolute property of the corporation as any man's property is his."

With reference to the suggestion in this last paragraph it may be observed that the court does not attempt to determine who are the proper parties to maintain a suit for the administration of the assets of an insolvent corporation. All that it decides is, that when a court of equity does take into its possession the assets of an insolvent corporation it will administer them on the theory that they in equity belong to the creditors and stockholders rather than to the corporation itself. In other words, and that is the idea which underlies all these expressions in reference to "trust" in connection with the property of a corporation, the corporation is an entity, distinct from its stockholders as from its creditors. Solvent, it holds its property as any individual holds his, free from the touch of a creditor who has acquired no lien; free also from the touch of a stockholder who, though equitably interested in, has no legal right to, the property. Becoming insolvent, the equitable interest of the stockholders in the property, together with their conditional liability

to the creditors, places the property in a condition of trust, first, for the creditors, and then for the stockholders. Whatever of trust there is arises from the peculiar and diverse equitable rights of the stockholders as against the corporation in its property and their conditional liability to its creditors. It is rather a trust in the administration of the assets after possession by a court of equity than a trust attaching to the property, as such, for the direct benefit of either creditor or stockholder.

(The learned Justice, after referring to the cases of *Wabash, St. Louis & Pacific Ry. v. Ham*, 114 U. S. 587; *Fogg v. Blair*, 133 U. S. 534, 541; *Hawkins v. Glenn*, 131 U. S. 319, 332, proceeded as follows:)

These cases negative the idea of any direct trust or lien attaching to the property of a corporation in favor of its creditors, and at the same time are entirely consistent with those cases in which the assets of a corporation are spoken of as a trust fund, using the term in the sense that we have said it was used.

The same idea of equitable lien and trust exists to some extent in the case of partnership property. Whenever, a partnership becoming insolvent, a court of equity takes possession of its property, it recognizes the fact that in equity the partnership creditors have a right to payment out of those funds in preference to individual creditors, as well as superior to any claims of the partners themselves. And the partnership property is, therefore, sometimes said, not inaptly, to be held in trust for the partnership creditors, or, that they have an equitable lien on such property. Yet, all that is meant by such expressions is the existence of an equitable right which will be enforced whenever a court of equity, at the instance of a proper party and in a proper proceeding, has taken possession of the assets. It is never understood that there is a specific lien, or a direct trust.

A party may deal with a corporation in respect to its property in the same manner as with an individual owner, and with no greater danger of being held to have received into his possession property burdened with a trust or lien. The officers of a corporation act in a fiduciary capacity in respect to its property in their hands and may be called to an account for fraud or sometimes even mere mismanagement in respect thereto; but as between itself and its creditors the corporation is simply a debtor and does not hold its property in trust, or subject to a lien in their favor, in any other sense than does an individual debtor. That is certainly the general rule, and if there be any exceptions thereto they are not presented by any of the facts in this case. Neither the insolvency of the corporation, nor the execution of an illegal trust deed, nor the failure to collect in full all stock subscriptions, nor, all together, gave to these simple contract

creditors any lien upon the property of the corporation, nor charged any direct trust thereon. * * *

Dismissed for want of jurisdiction.

Mr. JUSTICE BROWN and Mr. JUSTICE JACKSON dissented.⁷

AMES v. HESLET.

1897. 19 Mont. 188, 47 Pac. 805, 61 Am. St. 496.⁸

THE J. Chauvin Northwestern Furniture Company, a corporation of Butte, Montana, being unable to pay its debts and being threatened by W. A. Clark & Bro., one of its largest creditors, with an attachment suit, executed a general assignment for the benefit of its creditors in which said W. A. Clark & Bro. and several other creditors were preferred. Plaintiffs, as judgment creditors of the corporation, instituted an action to set aside this assignment. Judgment was rendered for the defendants, and plaintiffs appealed from the judgment and the order denying a motion for a new trial.

BUCK, J.—The determination of this appeal depends upon whether or not an insolvent corporation can make an assignment for the benefit of creditors, with preferences. Appellants' counsel insist that such an assignment is void. Their reasoning is substantially as follows: The assets of a corporation constitute a trust fund for its creditors, to which equitable liens at once attach in favor of each and every creditor upon insolvency. An insolvent corporation stands upon a different footing from an insolvent individual, because with insolvency the legal existence of the former is virtually at an end, while in the case of the latter he may subsequently accumulate property, and pay all his debts. They and the judges and text-writers who support this view urge that it is most unjust and illogical to hold that such a corporation, by an assignment of its entire property,—an act which in itself prevents any resumption of business operations,—should be permitted to favor one lienholder at the expense of another.

There are innumerable authorities replete with arguments for and against this contention, and it would be an act of supererogation for us in the present opinion to enter into an elaborate discussion of a subject which has been so thoroughly exhausted. For the details of the arguments pro and con, we cite the following, among the many called to our attention: 2 Mor. Priv. Corp., §§ 782, 786, 863; 5 Thompson on Corporations, §§ 6466, 6492-6496; Lyons-Thomas

⁷ Hageman v. Southern Electric R. Co. (1906) 202 Mo. 249, 100 S. W. 1081, *Accord*. See also Marvin v. Anderson (1901) 111 Wis. 387, 87 N. W. 226; But *cf.* City of Altoona v. Richardson Gas & Oil Co. (1910) 81 Kansas 717, 106 Pac. 1025, and note, 10 Columbia Law Rev. 479.—Eds.

⁸ Statement abridged.—Eds.

Hardware Co. v. Perry Stove Manufacturing Co. (Tex. Sup.) 22 Lawy. Rep. Ann. 802, note; s. c. 24 S. W. 16; Thompson v. Lumber Co. (Wash.) 30 Pac. 741; Rouse v. Bank, 46 Ohio St. 493, 22 N. E. 293; 4 Am. & Eng. Ency. Law (1st Ed.) page 220, note; 2 Cook, Stock, Stockh. & Corp. Law § 691. The great weight of authority is against appellants, and, in our opinion, is based on the better line of reasoning. In many of the cases cited, particularly those in federal courts, the statement is made that the assets of a corporation are a trust fund for its creditors; but it does not follow that even these courts intended by this expression to hold that creditors, by virtue of their mere attitude as such, have any lien upon the actual, tangible property of a corporation,—that property which belongs to it for its business operations, and which is primarily liable for its debts, as distinguished from any secondary liability of directors or stockholders. In our opinion, there is no such lien. The trust-fund doctrine, as invoked by appellants to sustain it, impresses us as an unsubstantial theory, constructed of judicial expressions selected without regard to their context or the facts in reference to which they were uttered. We refer, of course, to the cases where the adoption of the doctrine only appears inferentially. All this reasoning against upholding preferences in assignments by insolvent corporations should be addressed to legislatures, rather than the courts. The policy of allowing such preferences may be pernicious, even more so than that of allowing an insolvent individual to prefer creditors; but in the one class as in the other, it is for the legislature to decide the question of policy, not the courts. There is nothing in the statutes of Montana in force when this controversy arose forbidding such assignments; and, according to a large majority of the authorities, insolvent corporations and insolvent individuals are upon the same plane at common law in respect to them. As to any distinction between the status of a solvent and insolvent corporation in this connection, this court held in Gans v. Switzer, 9 Mont. 408, 24 Pac. 18, that the fact that an insolvent corporation had transferred all its property to one of its creditors, and abandoned business, did not dissolve it. For these reasons, the order denying the motion for a new trial and the judgment of the lower court are affirmed.

Affirmed.

PEMBERTON, C. J., and HUNT, J., concur.*

* Reichwald v. Commercial Hotel Co. (1883) 106 Ill. 439; Bank of Montreal v. Potts Salt & Lumber Co. (1892) 90 Mich. 345, 51 N. W. 512; Waggoner-Gates Milling Co. v. Ziegler-Zaiss Commission Co. (1895) 128 Mo. 473, 31 S. W. 28; *Accord*.

Rouse v. Merchants' Nat. Bank (1889) 46 Ohio St. 493, 22 N. E. 293, 5 L. R. A. 378n, 15 Am. St. 644; Lyons-Thomas Hardware Co. v. Perry Stove Mfg. Co. (1893) 86 Tex. 143, 24 S. W. 16; *Contra*. See note to last case in 22 L. R. A. 802.

Cf. Memphis Barrel etc. Co. v. Ward (1897) 99 Tenn. 172, 42 S. W. 13. 63 Am. St. 825; Sanford Fork & Tool Co. v. Howe, Brown & Co. Ltd. (1894)

McDONALD v. WILLIAMS.

1899. 174 U. S. 397, 43 L. ed. 1022, 19 Sup. Ct. 743.¹⁰

THIS suit was brought in the Circuit Court of the United States for the Southern District of New York by the plaintiff, as receiver of the Capital National Bank of Lincoln, Neb., for the purpose of recovering from the defendants, stockholders in the bank, the amount of certain dividends received by them before the appointment of a receiver.

The court below desired the instruction of this Court for the proper decision of the following questions:

First question. Can the receiver of a national bank recover a dividend paid not at all out of profits but entirely out of the capital, when the stockholder receiving such dividend acted in good faith, believing the same to be paid out of the profits, and when the bank, at the time such dividend was declared and paid, was not insolvent? (Second question omitted.)

MR. JUSTICE PECKHAM, after stating the facts, delivered the opinion of the court.

It will be noticed that the first question is based upon the facts that the bank, at the time the dividends were declared and paid was solvent, and that the stockholders receiving the dividends acted in good faith and believed that the same were paid out of the profits made by the bank.

The sections of the Revised Statutes which are applicable to the questions involved are set forth in the margin.¹

The complainant bases his right to recover in this suit upon the theory that the capital of the corporation was a trust fund for the

157 U. S. 312, 39 L. ed. 713, 15 Sup. Ct. 621; *Sutton Mfg. Co. v. Hutchinson* (1894) 63 Fed. 496.

See also *Thompson, Corps.* (2d ed.), secs. 3418-22.—Eds.

¹⁰ Statement abridged. Portions of opinion omitted.—Eds.

¹ SEC. 5199. The directors of any association may, semi-annually, declare a dividend of so much of the net profits of the association as they shall judge expedient; but each association shall, before the declaration of a dividend, carry one-tenth part of its net profits of the preceding half year to its surplus fund until the same shall amount to twenty per centum of its capital stock.

SEC. 5204. No association, or any member thereof, shall, during the time it shall continue its banking operations, withdraw, or permit to be withdrawn, either in the form of dividends or otherwise, any portion of its capital. If losses have at any time been sustained by any such association, equal to or exceeding its undivided profits then on hand, no dividend shall be made; and no dividend shall ever be made by any association, while it continues its banking operations, to an amount greater than its net profits then on hand, deducting therefrom its losses and bad debts. All debts due to any associations, on which interest is past due and unpaid for a period of six months, unless the same are well secured, and in process of collection, shall be considered bad debts within the meaning of this section. But nothing in this section shall prevent the reduction of the capital stock of the association under section 5143.

payment of creditors entitled to a portion thereof, and having been paid in the way of dividends to the shareholders that portion can be recovered back in an action of this kind for the purpose of paying the debts of the corporation. He also bases his right to recover upon the terms of section 5204 of the Revised Statutes.

We think the theory of a trust fund has no application to a case of this kind. When a corporation is solvent, the theory that its capital is a trust fund upon which there is any lien for the payment of its debts has in fact very little foundation. No general creditor has any lien upon the fund, under such circumstances, and the right of the corporation to deal with its property is absolute so long as it does not violate its charter or the law applicable to such corporation.

(The learned justice, after referring to several cases, proceeded.)

These cases, while not involving precisely the same question now before us, show there is no well-defined lien of creditors upon the capital of a corporation while the latter is a solvent and going concern, so as to permit creditors to question, at the time, the disposition of the property.

The bank being solvent, although it paid its dividends out of capital, did not pay them out of a trust fund. Upon the subsequent insolvency of the bank and the appointment of a receiver, an action could not be brought by the latter to recover the dividends thus paid on the theory that they were paid from a trust fund, and therefore were liable to be recovered back.

It is contended on the part of the complainant, however, that if the assets of the bank are impressed with a trust in favor of its creditors when it is insolvent, they must be impressed with the same trust when it is solvent; that the mere fact that the value of the assets of the corporation has sunk below the amount of its debts, although as yet unknown to anybody, cannot possibly make a new contract between the corporation and its creditors. In case of insolvency, however, the recovery of the money paid in the ordinary way without condition is allowed, not on the ground of contract to repay, but because the money thus paid was in equity the money of the creditor; that it did not belong to the bank, and the bank in paying could bestow no title in the money it paid to one who did not receive it bona fide and for value. The assets of the bank, while it is solvent, may clearly not be impressed with a trust in favor of creditors, and yet that trust may be created by the very fact of the insolvency, and the trust enforced by a receiver as a representative of all the creditors. But we do not wish to be understood as deciding that the doctrine of a trust fund does in truth extend to a shareholder receiving a dividend, in good faith believing it is paid out of profits, even though the bank at the time of the payment be in fact insolvent. That question is not herein presented to us, and we express no opinion in regard to it. We only say, that if such a dividend be recoverable, it would be on the principle of a trust fund.

Insolvency is a most important and material fact, not only with

individuals but with corporations, and with the latter as with the former the mere fact of its existence may change radically and materially its rights and obligations. Where there is no statute providing what particular act shall be evidence of insolvency or bankruptcy, it may be and it sometimes is quite difficult to determine the fact of its existence at any particular period of time. Although no trust exists while the corporation is solvent, the fact which creates the trust is the insolvency, and when that fact is established at that instant the trust arises. To prove the instant of the creation may be almost impossible, and yet its existence at some time may very easily be proved. What the precise nature and extent of the trust is, even in such case, may be somewhat difficult to accurately define, but it may be admitted in some form and to some extent to exist in a case of insolvency.

Hence it must be admitted that the law does create a distinction between solvency and insolvency and that from the moment when the latter condition is established the legality of acts thereafter performed will be decided by very different principles than in a case of solvency. And so of acts committed in contemplation of insolvency. The fact of insolvency must be proved in order to show the act was one committed in contemplation thereof.

Without reference to the statute, therefore, we think the right to recover the dividend paid while the bank was solvent would not exist.

But it is urged on the part of the complainant that section 5204 of the Revised Statutes makes the payment of a dividend out of capital illegal and ultra vires of the corporation and that money thus paid remains the property of the corporation, and can be followed into the hands of any volunteer.

The section provides that "no association, or any member thereof, shall, during the time it shall continue its banking operations, withdraw, or permit to be withdrawn, either in the form of dividends or otherwise, any portion of its capital." What is meant by this language? Has a shareholder withdrawn or permitted to be withdrawn in the form of a dividend any portion of the capital of the bank when he has simply and in good faith received a dividend declared by a board of directors of which he was not a member, and which dividend he honestly supposed was declared only out of profits? Does he in such case within the meaning of the statute withdraw or permit to be withdrawn a portion of the capital? The law prohibits the making of a dividend by a national bank from its capital or to an amount greater than its net profits then on hand, deducting therefrom its losses and bad debts. The fact of the declaration of a dividend is in effect the assertion by the board of directors that the dividend is made out of profits. Believing that the dividend is thus made, the shareholder in good faith receives his portion of it. Can it be said that in thus doing he withdraws or permits to be withdrawn any portion of the capital of the corporation? We think he does not

withdraw it by the mere reception of his proportionate part of the dividend. The withdrawal was initiated by the declaration of the dividend by the board of directors, and was consummated on their part when they permitted payment to be made in accordance with the declaration. We think this language implies some positive or affirmative act on the part of the shareholder by which he knowingly withdraws the capital or some portion thereof, or with knowledge permits some act which results in the withdrawal, and which might not have been so withdrawn without his action. The permitting to be withdrawn cannot be founded upon the simple receipt of a dividend under the facts stated above.

One is not usually said to permit an act which he is wholly ignorant of, nor would he be said to consent to an act of the commission of which he had no knowledge. Ought it to be said that he withdraws or permits the withdrawal by ignorantly yet in entire good faith receiving his proportionate part of the dividend? Is each shareholder an absolute insurer that dividends are paid out of profits? Must he employ experts to examine the books of the bank previous to receiving each dividend? Few shareholders could make such examination themselves. The shareholder takes the fact that a dividend has been declared as an assurance that it was declared out of profits and not out of capital, because he knows that the statute prohibits any declaration of a dividend out of capital. Knowing that a dividend from capital would be illegal, he would receive the dividend as an assurance that the bank was in a prosperous condition and with unimpaired capital. Under such circumstances we cannot think that Congress intended by the use of the expression "withdraw or permit to be withdrawn, either in the form of dividends, or otherwise," any portion of its capital, to include the case of the passive receipt of a dividend by a shareholder in the bona fide belief that the dividend was paid out of profits, while the bank was in fact solvent. We think it would be an improper construction of the language of the statute to hold that it covers such a case. * * *

We may concede that the directors who declared the dividend under such circumstances violated the law, and that their act was therefore illegal, but the reception of the dividend by the shareholder in good faith, as mentioned in the question, was not a wrongful or designedly improper act. Hence the liability of the shareholder should not be enlarged by reason of the conduct of the directors. They may have rendered themselves liable to prosecution, but the liability of the shareholder is different in such a case, and the receipt of a dividend under the circumstances is different from an act which may be said to be generally illegal, such as the purchase of stock in one national bank by another national bank for an investment merely, which is never proper. *Concord First National Bank v. Hawkins*, just decided, *ante*, 364.

The declaration and payment of a dividend is part of the course of business of these corporations. It is the thing for which they are

established, and its payment is looked for as the appropriate result of the business which has been done. The presumption of legality attaches to its declaration and payment, because declaring it, is to assert that it is payable out of the profits. As the statute has provided a remedy under section 5205 for the impairment of the capital which includes the case of an impairment produced by the payment of a dividend, we think the payment and receipt of a dividend under the circumstances detailed in the question certified do not permit of its recovery back by a receiver appointed upon the subsequent insolvency of the bank.

The facts in the various English cases cited by counsel for complainant are so entirely unlike those which exist in this case that no useful purpose would be subserved by a reference to them. Not one holds that a dividend declared under such facts as this case assumes can be recovered back in such an action as this. * * *

*The first question will be certified in the negative.*¹¹

MILLS v. NORTHERN RAILWAY, ETC., CO.

1870. L. R. 5 Chan. App. Cas. 621.¹²

APPEAL from an order of Vice-Chancellor Stuart, granting an interlocutory injunction against the Northern Railway of Buenos Ayres Company, Ltd.

The directors had issued a report recommending that certain sums which had been paid out of revenue, and ascribed in the accounts of the company to revenue account, should be treated as payments on capital account and considered as having been borrowed for the purpose of capital from revenue, and that the capital account should be reimbursed out of the proceeds to be raised by means of the issue of debenture stock. The report also recommended the conversion of the tramway from the custom-house at Buenos Ayres to the principal station into a railway adapted for locomotive engines.

The suit was brought on behalf of a firm of contractors, who had done some work for the railway company. The bill prayed for an account and payment of what was due to the plaintiffs under the contract and for other works, and for an injunction to restrain the

¹¹ In *Hayden v. Williams* (1899) 96 Fed. 279, 37 C. C. A. 479, held that the receiver of the bank could recover from a stockholder all dividends declared and paid after the bank became insolvent so far as necessary to meet the demands of creditors. Lacombe, Circuit Judge, after referring to the Supreme Court's negative answer to the question certified, said: "No question was propounded as to the dividends paid when the bank was actually insolvent. as we had no doubt the receiver could recover them in a proper action." (p. 283) See note, 8 Columbia Law Rev. 303.

See *Davenport v. Lines* (1899) 72 Conn. 118, 44 Atl. 17; *Dykman v. Keeney* (1899) 160 N. Y. 677, 54 N. E. 1090.—Eds.

¹² Statement abridged. Portion only of the opinion is given.—Eds.

company from carrying out the proposal in the report and from issuing any debenture stock and from declaring any dividend until they had made provision for paying what was due to the plaintiffs; also, from converting the tramway into a railway until the company had duly increased their capital.

LORD HATHERLEY, L. C.—The Vice-Chancellor appears to have formed his judgment in this case, partly at least, upon the view which he took that one of the Plaintiffs, Mr. Mills, was a shareholder in the company, and therefore had a right to interfere. But, so far as the case rests on the single fact of the Plaintiffs being creditors of the company, it seems to me hardly capable of argument. Work is done for a limited company; no engagement is taken from them by way of security; no debenture or mortgage is granted by them; but the work is done simply on the credit of the company. The only remedy for a creditor in that case is to obtain his judgment and to take out execution; or it may be that he may have a power, if the case warrants it, of applying to wind up the company. But it is wholly unprecedented for a mere creditor to say, "Certain transactions are taking place within the company, and dividends are being paid to shareholders which they are not entitled to receive, and therefore I am entitled to come here and examine the company's deed, to see whether or not they are doing what is *ultra vires*, and to interfere in order that, as by a bill *quia timet*, I may keep the assets in a proper state of security for the payment of my debt whensoever the time arrives for its payment."

The case must have occurred, of course, many years ago, before joint stock companies were so abundant, but certainly within the last twenty or thirty years the money due to creditors must have been many millions, and the number of creditors must have been many thousands; yet I have never before heard—and I asked in vain for any such precedent—of any attempt on the part of a creditor to file a bill of this description against a company, claiming the interference of this Court on the ground that he, having no interest in the company, except the mere fact of being a creditor, is about to be defrauded by reason of their making away with their assets. It would be a fearful authority for this Court to assume, for it would be called on to interfere with the concerns of almost every company in the kingdom against which a creditor might suppose that he had demands, which he had not established in a court of justice, but which he was about to proceed to establish. If there is this power in any case, of course it would apply not only to the raising of money by debentures and to paying shareholders, but it would extend to an interference in every possible way with the dealings of the company. * * *

The motion for the injunction was denied with costs.

*Order reversed.*¹²

¹² See also *O'Conner Mining & Mfg. Co. v. Coosa Furnace Co.* (1891) 95

Section 2.—Relation Between Creditor and Director.**A—AT COMMON LAW.****BATH v. STANDARD LAND COMPANY, LIMITED.**1911. (1911) 1 Ch. Div. 618.¹

APPEAL from a decision of Neville, J. (1910) 2 Ch. 408.

The only question raised by this appeal which calls for any detailed report was whether a limited company which had undertaken the management of an estate upon certain terms was entitled to charge for the professional services of some of its directors who had been employed to do some part of the management.

Quarterly accounts were sent regularly to the plaintiff, but he did not agree to them, and eventually he brought the present action against the company claiming that the accounts might be taken under the directions of the Court on the ground that they contained improper charges.

It appeared that one of the directors, a Mr. May, was a solicitor and a member of the firm of May, Sykes & Co., and his firm were employed professionally by the defendant company in matters connected with the estates, and their bills of costs, which contained profit items, were paid by the company. Mr. Corke was an estate agent and surveyor and was employed by the defendant company at a salary of £200 per annum to manage certain sand and gravel pits comprising part of the estates, and the business in connection with these pits occupied a large portion of his time and was carried on at a considerable profit. The objection to this charge was not pressed on the appeal. Mr. Snelling was an auctioneer, and was always employed by the defendant company on all sales of the property and was paid the usual commission. Mr. Reeves was a chartered accountant, and, in addition to his salary as secretary of the company, was paid £80 per annum for keeping the books of account of the estates, which were very complicated. It was not alleged that

Ala. 614, 10 So. 290, 36 Am. St. 251; *Force v. Age-Herald Co.* (1903) 136 Ala. 271, 33 So. 866; *Pond v. Framingham etc. R. Co.* (1881) 130 Mass. 194.

In the case last cited, Morton, J., said: "The bill is an attempt by a creditor to restrain his debtor (the railroad company) from making what is alleged to be an improvident contract. The rights of the parties are governed by the rules of the common law. The plaintiffs as creditors might by an attachment have obtained security which would take precedence of the contemplated lease; but if they could not, the court has no power to restrain the debtor from making a disposition of his property which is permitted by the common law, unless fraud or a breach of trust is alleged and shown. The allegation that the defendant corporation is insolvent does not aid the plaintiffs. In the absence of any statute giving the power, this court has no authority to act as a court of insolvency for the liquidation of the affairs of an insolvent railroad corporation." (p. 195).—Eds.

¹ Statement abridged. Portion of Fletcher-Moulton's dissenting opinion omitted.—Eds.

these payments were in themselves unfair or unreasonable, but it was objected that they could not be charged against the plaintiff.

COZENS-HARDY, M. R.—Neville, J., has declared that the company are not entitled to make any charge for or in respect of any profit or remuneration to the directors or to any of them, or to any firm of which any such director was a member for anything done by such directors or any of them, or by any firm of which such directors or any of them were members at the time of the doing thereof in relation to the agreement. Now it has not been disputed that the company stood in a fiduciary relation to the plaintiff, and in my view it is not very important to ascertain precisely the nature of that relation. During all the period in question the company were mortgagees in possession. They may also be regarded as managers of a joint adventure. However that may be, it is clear that not one penny of profit can be claimed by the company beyond that which is expressly provided for in the agreement. But I fail to see on what ground the company can be charged with profits which in fact the company did not receive, and which were received by the directors.

Directors stand in a fiduciary relation to the company, but not to a stranger with whom the company is dealing. It is of course true that a company acts through its directors. But that does not involve the proposition that if a breach of trust is committed by a company, acting through its board, a beneficiary can maintain any action against the directors in respect of such breach of trust. Of course I except the case where trust property can be followed into the hands of a director, or of any stranger with notice. No such point arises here.

It is argued that it was an implied term of the agreement that all the services of the directors should, as between the plaintiff and the company, be rendered gratuitously. Another way in which the same result was sought to be reached was by suggesting that, although solicitors and auctioneers might be employed by the company and paid for their services, it was an implied term that no director should be so employed. I can find no foundation for such argument. Moreover, a breach of such implied term (if any) would give rise to a claim for damages only, which would not be measured by the amount of profits earned by the director or his firm. On principle I think it is clear that, in an action of this nature to which the directors are not made parties, it cannot be right to treat their profits as sums improperly received by the company, or improperly paid away by the company.

But it is said that there are two authorities which justify the declaration appealed against. *Nicholson v. Tutin* (3 K. & J. 159.), before Wood V.-C., creates no difficulty, and indeed it seems to me to be a plain case. Tutin and Watson were trustees of a creditor's deed, the trusts of which were being administered under the decree of the Court. In the accounts carried into chambers by the trustees, a

sum of £450 was charged by Watson as commission for collecting the rents. Watson alleged that, after the execution of the creditor's deed, he was appointed agent of mortgagees, who had no express power to appoint a receiver, to receive the rents. But this was held no justification for a charge of the £450 against the plaintiff Nicholson, between whom and Watson there was a direct fiduciary relation. It has no bearing upon the present case. The case of *Kavanagh v. Workingman's Benefit Building Society* ([1896] 1 L. R. 56) is no doubt directly in point. The defendants were mortgagees in possession, the mortgage deed containing a power to appoint a receiver. The defendants appointed one of their directors receiver to collect the rents. The appointment was by deed under the seal of the corporation, in pursuance doubtless of a resolution of the board of directors. Under a redemption decree, the defendants charged commission at 5 per cent. for collecting the rents. The Court of Appeal in Ireland held that the company could not claim any commission paid to the director. Lord Ashbourne thought the director could not claim commission against the mortgagor, because he might have voted for his own appointment. FitzGibbon, L. J., thought the disability arose from inconsistency between duty and interest. He is reported to have used these words ([1896] 1 L. R. 58): "Public policy and equitable doctrine are both against allowing the claim, which could only be made for the pecuniary benefit of one director through the action of the board of directors, against the interest either of the company or of the mortgagor, to both of whom every director stands in a fiduciary relation." Barry, L. J., said it made no difference that the director was not the mortgagee himself, but a "part of the corporation." And Walker, L. J., substantially agreed with FitzGibbons, L. J. With all respect to the very learned judges who decided that case, I am unable to follow their reasoning. It seems to me fallacious to say that every director stands in a fiduciary relation to the mortgagor. The conflict between interest and duty only arises where a fiduciary relation exists between the parties. Reference was also made to *Powell & Thomas v. Evan Jones & Co.* ([1905] 1 K. B. 11), but I am unable to discover that it in any way assists the plaintiff in his contention. I base my decision upon the broad principle that directors stand in a fiduciary position only to the company, not to creditors of the company, not even to individual shareholders of the company, still less to strangers dealing with the company. This principle applies equally whether the relation between the company and the stranger is one purely of contract, such as principal and agent, or is one of trustee and cestui que trust. To speak of directors as the "brains" of the company or the "hands" of the company is only to use words which have no definite meaning in this connection.

With great respect to Neville, J., who followed the Irish decision, I am unable to concur in his view. I think the declaration as to the profits received by directors should be struck out. But in order to

avoid mistakes it is desirable to add words to the following effect: "But the omission of this declaration is without prejudice to any question as to the propriety of employing any such director or his firm, or any other person in any particular transaction, or as to the amount of remuneration paid in respect thereof."

As the appellants have partly failed and partly succeeded, I think there should be no costs of the appeal.

FLETCHER MOULTON, L. J.— * * * There is no lack of boldness in the propositions contended for by the appellants. They contend that the directors of a company which is acting in a fiduciary relation to an individual—in short, in the position of a trustee towards him—are merely in the position of agents of a trustee, and that it is a settled principle of English law that an agent of a trustee is not in any fiduciary relation to the cestuis que trust. Accordingly they say that the directors of the defendant company had no duty whatever to the plaintiff. They admit that the company of which they were directors was in the position of a mortgagee in possession, and I do not think that they dispute that its position under the agreement of April 20, 1893, also was one of such a fiduciary character that it was liable to account to the plaintiff and could make no personal profit out of its actual administration of the estate. But they maintain that these facts entail no consequences so far as the directors of the company are concerned, that their position was simply that of agents for the company, and that, provided the company itself did not object, they might sell the trust property to members of their body, allow to one another commissions in respect of sales, etc., of the trust property, and employ one another for reward on such terms as they should think proper in respect of the development and realization of that property. They contend that the fiduciary relations existed between the company and the plaintiff only, and that the directors were entirely unaffected by the existence of those relations, by the fact that they were administering the property for the company as a trustee, and by their complete knowledge both of the position of the company and the relations in which it stood to the plaintiff.

It would be difficult to exaggerate the importance of the questions thus raised, especially at a time when there is an increasing tendency to employ corporate bodies in the execution of trusts. The strength of the position of cestuis que trust hitherto has been that no profit could be made by those administering the trust out of such administration, so that no question of self-interest could divert the trustee from the duty to use his powers solely in the interests of cestuis que trust. But if such principles are wholly inapplicable to the individuals who, in the case of a trustee company, are the persons really administering the trust, i. e., the directors, and if they can use the powers which are thus in their hands to their own personal advantage without incurring any liability to the cestuis que trust, the whole security of the position is gone. Yet this is what is contended

for by the appellants. Suppose that in such a case there is a sale to the directors or some of them. The appellants argue that inasmuch as the company does not pocket the profits made by the directors there is no breach of trust. So far as the directors themselves are concerned it is contended that they have no duty whatever to the cestuis que trust, who cannot therefore impeach the sale even though the purchasers have a hand in fixing the price. They contend that the directors are liable to the company and to it alone, and hence that if the company does not complain (and the directors will decide whether it shall do so or not) the cestuis que trust are helpless except so far as they can make out a case of negligence leading to damage—a very poor substitute for the protection afforded by the principle of equity that no one may allow himself to be in a position in which his interest conflicts with his duty.

It is needless to say that if propositions of so wide a character as those contended for by the appellant can be established the declaration appealed against is wholly wrong. But in my opinion they cannot be established. There is, in my opinion, a fundamental fallacy in the whole of the argument addressed to us by counsel for the appellant on this part of the case. It is that they have founded the proposition that a man does not come into fiduciary relations with the cestuis que trust merely by becoming an agent of the trustee (a proposition of undoubted validity) with the proposition that an agent to the trustee cannot stand in a fiduciary relation to the cestuis que trust. This is to my mind as grave an error as for a criminal lawyer to maintain the proposition that a fact that is not sufficient to secure a conviction is sufficient to necessitate an acquittal. In order to establish a fiduciary relation between the cestuis que trust and an agent of the trustee you must look at the facts of the case and see whether they establish such a relationship. It is impossible to say generally whether an agent of a trustee is in a fiduciary relation to the cestuis que trust, but it is not only possible, but correct, to say that if nothing is present but the fact that he is an agent of the trustee, that alone does not suffice to make him responsible to the cestuis que trust. In such matters a man's responsibilities depend on the acts which he does and the knowledge that he possesses at the time when he does them. This is true whether a man be an agent of a trustee or not. His being such agent does not shelter him from the responsibilities flowing from the knowledge he actually possesses, whether that knowledge has come to him by virtue of his position or aliunde. If it is such that it would suffice to make a third person liable to the cestuis que trust for the acts done by him, his being an agent to a trustee is no defence against his being held to be so liable. * * *

CASSIDY v. UHLMANN.

1902. 170 N. Y. 505, 63 N. E. 534.*

APPEAL from a judgment of the Appellate Division of the Supreme Court in the first judicial department, entered November 17, 1900, affirming a judgment in favor of plaintiff entered upon a verdict and an order denying a motion for a new trial.

The nature of the action and the facts, so far as material, are stated in the opinion.

WERNER, J.—The plaintiff, as assignee of the claims of several depositors in the Madison Square Bank, brought this action against the president and two directors thereof to recover damages for their alleged fraud and deceit in directing and permitting said bank to remain open for the transaction of its regular business after it had become hopelessly insolvent, and in directing and permitting said bank to receive the deposits made by plaintiff's assignors while said bank was in said insolvent condition and with full knowledge thereof. The complaint charges, in substance, that the Madison Square Bank was a moneyed corporation organized under the laws of this state, and prior to August, 1893, engaged in the banking business in the city of New York; that on the 7th and 8th of August, 1893, the plaintiff's assignors deposited certain moneys with said bank; that it was then hopelessly insolvent and permanently closed its doors at the end of banking hours on the 8th day of August, 1893; that the defendant Blaut as president of said bank, and the defendants McDonald and Uhlmann as directors thereof, constituting a committee having the charge, management, direction and actual control of said bank and having knowledge of its insolvency, did direct the same to be kept open for the regular transaction of its business for the purpose of inducing depositors to deposit moneys therein, and with that purpose and intention did represent to the depositors of said bank that it was solvent and could properly and lawfully accept deposits; that said representations were false; that while said bank was insolvent it received the moneys of the plaintiff's assignors; that this was done with the consent, direction, procurement and instigation of said defendants who wrongfully concealed from said depositors the actual condition of said bank to their damage to the extent of their said deposits, less the dividends paid to apply thereon by the receiver of said bank. Service of the summons herein was never made upon said Blaut, the president of said bank. McDonald, although served, died before the trial of the action, and it has not been revived as against his personal representatives. The appellant Uhlmann is, therefore, the sole defendant. He presented no evidence.

The evidence given in support of the allegations of the complaint

* Dissenting opinion of Martin J. in which Parker, C. J. and Haight, J. concurred, omitted, also portion of opinion of Werner J.—Eds.

is substantially as follows: (After summarizing the evidence and stating that the findings of fact were (1) that the deposits, under which the plaintiff claims, were made in the Madison Square Bank on the seventh and eighth days of August, 1893; (2) that said bank was then insolvent; (3) that the defendant, then a director of said bank, had knowledge of such insolvency; (4) that the defendant, with knowledge of such insolvency, took part in directing the receipt of deposits by said bank, the learned justice proceeded:)

The theory upon which the action was brought, and upon which the defendant has been held liable in the courts below, is that by taking part in directing the receipt of deposits by said bank, knowing that it was insolvent, the defendant was guilty of a fraud by which the plaintiff's assignors were damaged and which gave them, or their assignee, a cause of action. This charge of fraud is predicated not alone upon the ordinary duties with which the defendant was charged by virtue of his office as a director of the bank, but upon those duties in connection with others, which he is said to have voluntarily assumed by his course of conduct during the last days of the bank. It is evident that we can arrive at no just conclusion upon the questions involved in the action without an approximately correct understanding of the relations, to each other, of the parties interested in the controversy.

The ordinary relation between a bank and its depositors is that of debtor and creditor. (*Cragie v. Hadley*, 99 N. Y. 133; *Commercial Bank v. Hughes*, 17 Wend. 94; *Met. Nat. Bank v. Loyd*, 90 N. Y. 530; *Aetna Nat. Bank v. Fourth Nat. Bank*, 46 N. Y. 86; *Crawford v. West Side Bank*, 100 N. Y. 53; *Fowler v. Bowery Savings Bank*, 113 N. Y. 453.) This is because cash when deposited ceases to be the money of the depositor and becomes the property of the bank. A different rule obtains, however, when by reason of fraud or insolvency, the title to the deposited money does not pass. In such a case the bank becomes a trustee *ex maleficio* and, of course, the relation of trustee and *cestui que trust* is created. (*Atkinson v. Rochester Printing Co.*, 114 N. Y. 168.) So far as creditors are concerned, the relation between a bank and its directors is that of principal and agent. (*Briggs v. Spaulding*, 141 U. S. 132.) There is also a qualified trust relation between the directors of a bank and its stockholders on the one hand, and between such directors and the bank's creditors on the other. Since the affairs of a bank are necessarily subject to the exclusive control of its directors, the acceptance of the office of director carries with it the implied and inherent obligation to perform the duties thereof in such a way as to promote the best interests of the stockholders. (*Duncomb v. N. Y., H. & N. R. R. Co.*, 84 N. Y. 199; *Cumberland Coal and Iron Co. v. Parish*, 42 Md. 599.) So long as a bank is solvent and continues its business in the regular and proper way, its directors are neither agents nor trustees of the creditors. But when a bank is insolvent its directors, who continue to serve as such be-

come trustees for the creditors, because they are the custodians of the bank's assets, which constitute a trust fund for the payment of its debts. (*Beach v. Miller*, 130 Ill. 162; *Haywood v. Lincoln Lumber Co.*, 64 Wis. 639; *Richards v. N. H. Ins. Co.*, 43 N. H. 263.) An incorporated bank must, of course, be conducted through the intervention of duly authorized officers and agents. The board of directors of a bank has the general superintendence and active management of all its concerns, and, for all practical purposes, the board is the corporation. As a general rule a board of directors must act as a board. But, since directors do not exercise a delegated authority in the sense which applies to other officers and agents, it is clear that a board of directors may delegate some of its powers to committees and individuals selected from the board. This is common practice in the management of banks as well as other corporations. Since a board of bank directors is composed of individuals it is manifest that each director sustains a distinct relation, not only to his bank, but to its stockholders and depositors. For obvious reasons the duties which attach to this relation cannot be precisely defined. They cannot be the same under all circumstances; nor can they be imposed with unvarying exactness upon all directors alike. Again, applying a general rule, bank directors are bound to administer the affairs of a bank according to the terms of its charter, in good faith and with reasonable care and diligence. (*First Nat. Bank v. Ocean Nat. Bank*, 60 N. Y. 278.) Those who deal with a bank have the right to expect reasonable diligence and good faith at the hands of its directors. If the latter fail in either, they violate a duty which they owe to both stockholders and depositors. Justice and public policy require that when one voluntarily takes the position of bank director he should exercise at least the same degree of care that men of common prudence exercise in their own affairs. (*Hun v. Cary*, 82 N. Y. 65.) * * *

It is urged on defendant's behalf: 1st. That the affirmation of solvency implied in keeping the bank open for the receipt of deposits was the affirmation of the bank and not of the defendant. 2nd. That since a corporate bank can only act through its board of directors, as a board, the defendant's acts were without power and that there can be no duty where there is no power. 3rd. That defendant did nothing as a result of which the bank was kept open or the receipt of deposits was continued. It is true that, primarily, the affirmation of the bank's solvency implied in keeping it open for the receipt of deposits, was the act of the bank. It is equally true that a corporate bank usually acts through its board of directors. We think it is not true that the fraud in this transaction was the fraud of the bank alone; nor can we admit the soundness of the argument that the defendant had neither power nor duty in the premises. Power and duty, even when strictly correlative, are never exact and unvarying unless they arise out of fixed, clearly defined and unchanging conditions. Such conditions rarely exist in any

phase of commercial activity. This is particularly true of banking. The executive officers of corporate banks are necessarily vested with large discretionary powers. In delegating some of its powers to others, a board of directors does not abdicate its other functions, nor do the individual members of the board become mere automata, bereft of the power of speech and action, except when the mechanism of the board is set in motion. There are many emergencies which call for individual action by directors, although no formal authority has been conferred. If a bank director should discover a fire in his banking house he would not wait for a formal meeting of the board of directors to authorize him to make an attempt to extinguish the fire or to call out the fire department. If a theft of the bank's money should be attempted in the presence of a single director, under such circumstances that his prompt interference would easily prevent its consummation, no one would seriously question that director's power and duty in the premises, because the charter and by-laws of the bank contained no provision to meet such an emergency. If, in such a case, a director should try to do his obvious duty and fail, he would of course incur no liability. But suppose he should actually participate with a bank officer, of superior or equal grade, in starting the fire or committing the theft, could there be an utter absence of duty and liability, simply because there was an apparent lack of formal power? * * *

In the case at bar we are dealing with fiduciary relations. The defendant was the director of an insolvent bank and the plaintiff's assignors were innocent depositors. The insolvency of the bank made the directors trustees for its creditors. While courts should be careful to establish no rule that will impose upon bank directors harsh and unjust burdens, they should not be over nice in guarding them with the technicalities of evidence when charged with dishonesty or negligence in the performance of their official duties. Courts should remember that when men accept the honors which attach to such offices they also assume some duties to the stockholders and depositors whom they represent. In this age of banks and banking, confidence is the cornerstone of the whole business structure. Once let it be known that a bank director can be made liable for nothing that is not done by an organized board of directors, and confidence in banks will be put to a crucial test, and a dishonest director will never be at a loss for means of escape.

*Judgment affirmed.*³

³ Delano v. Gardner Case (1887) 121 Ill. 247, 12 N. E. 676, 2 Am. St. 81, Accord. Union National Bank v. Hill (1898) 148 Mo. 380, pp. 393-398, 49 S. W. 1012, 17 Am. St. 615, Contra. Cf. Van Weel v. Winston (1885) 115 U. S. 228, 247, 29 L. ed. 384, 388, 6 Sup. Ct. 22.—Eds.

BEACH v. MILLER.

1889. 130 Ill. 162, 22 N. E. 464.*

MR. JUSTICE CRAIG delivered the opinion of the Court:

IN order to get a correct understanding of the questions presented by the record, a brief statement of the facts seems to be required. The Rock River Packing Company is a corporation, organized in 1881, with a capital stock of \$16,000, the incorporators being James A. Ingersoll, Edward H. Sears, William N. Herman, and Joseph T. Miller, the plaintiff here. The corporation was formed for "packing, pickling, canning and bottling of meats, vegetables and fruits, and dealing in the same," and was located at Sterling, where it provided itself with a factory and warehouse, in which its business was transacted. During the spring and summer of 1885 the corporation borrowed of Miller, who was then a director, money to be used in its business, amounting to the sum of \$2,000. To secure Miller for the money loaned, the corporation executed and delivered to him its four judgment notes, one dated May 30, 1885, amount \$500; one July 6, 1885, amount \$500; and one for \$1,000, on August 17, 1885. On the 16th day of October, 1885, these notes being due and unpaid, the president and secretary of the corporation sold Miller 80,000 cans and a small quantity of tin for \$1,877, to be applied as a payment on the notes. On the same day, Ingersoll, president and secretary of the corporation, leased Miller two small rooms in the north end of the company's warehouse. On the morning of the 17th, all property belonging to the company was removed from the two rooms, and the possession was turned over to Miller. Miller placed the goods purchased in the rooms, and nailed up the doors communicating with other parts of the warehouse, and placed new locks on the other doors. On the 17th day of October, 1885, the corporation delivered to E. W. Blatchford & Co. a judgment note for \$1,415.40, upon which judgment was entered. On the 23d day of October an execution issued on the judgment, and on the 24th, defendant Beach, as sheriff, and defendant Keefer, as deputy sheriff, levied on the goods which had been purchased by Miller.

In the circuit court it was contended that the sale of the goods from the Rock River Packing Company to Miller was fraudulent as against creditors, and being fraudulent, the goods were liable to be seized and sold by the sheriff on the execution in favor of Blatchford & Co., against the Rock River Packing Company. For the purpose of showing the sale fraudulent, the defendants offered to prove that the Rock River Packing Company was, at the time of the sale, insolvent; that on the 16th day of October, 1885, the company executed a mortgage on its real estate for \$7,000, to three of its directors; that the company turned over \$1,000 of its accounts to the Sterling National Bank, to apply on a debt due from the com-

* A portion of the opinion omitted.—Eds.

pany to the bank, which debt was secured by three of the directors of the company; that between the 16th and the 23d days of October, the corporation sold the product of their manufacture to a certain party in Chicago. This offered evidence, and other evidence of a like import, was ruled out by the court, and the decision is relied upon as error. We are of opinion that the court erred in excluding this evidence from the jury. If, at the time this sale was made, the corporation was insolvent, or if, at or about the time when the sale was made, large mortgages were placed on all of the property owned by the corporation, so that it had no property left liable to execution, these were facts proper for the consideration of the jury on the question whether the sale to Miller was fraudulent or made in good faith. What weight should be given to this character of evidence, was a question for the jury. We only determine that it was competent evidence for the consideration of the jury, on the issue presented by the pleadings. Where the good faith of a sale of property is attacked, it is always competent to prove that the vendor was embarrassed or insolvent. *Geisendorf v. Eagles*, 106 Ind. 38; *Bump on Fraud. Con.* 591.

While a corporation remains solvent, we perceive no reason why a director, with the knowledge of the stockholders, may not deal with the corporation, loan it money, take security or buy property of it, in like manner as a stranger; but whether a director in an insolvent corporation may purchase the assets in payment of a debt, and thus secure a preference over other creditors, presents a different question. So long as a corporation remains solvent, its directors are agents or trustees for the shareholders. They owe no duties or obligations to others. But the moment a corporation becomes insolvent, its directors occupy a different relation. The assets of the corporation must then be regarded as a trust fund for the payment of all its creditors, and the directors occupy the position of trustees, and, a fiduciary relation then existing, they may, with propriety, be prohibited from purchasing the trust property. The relation that directors occupy to the property of a corporation is well stated in *Ogden v. Murray*, 39 N. Y. 202, as follows: "The appellants and their associates were not in a situation permitting them to secure to themselves a personal advantage in the matter. The stockholders and creditors were entitled, not only to their vote in the board, but to their influence and argument in the discussion which led to the passage of the resolution in pursuance of which they took title as trustees. This brings the case within the rule which rests in the soundest wisdom, and is sustained by the best consideration of the infirmities of our human nature, and called for by the only safe protection of the interests of *cestuis que trust* or beneficiaries, viz., that trustees and persons standing in similar fiduciary relations shall not be permitted to exercise their powers, and manage or appropriate the property of which they have control, for their own profit or emolument,—or, as it has been expressed, shall not take

advantage of their situation to obtain any personal benefit to themselves at the expense of their *cestuis que trust*." See, also, *Drury v. Cross*, 7 Wall. 299.

After a careful examination of the authorities, we are inclined to the opinion, that if this corporation was insolvent at the time of the sale, Miller, who was a director, could not lawfully purchase the property in satisfaction of his own debt to the exclusion of other creditors, but he took the property charged with the trust in favor of other creditors, which may be enforced in an appropriate action. Miller, being a creditor, would doubtless be entitled to share with the other creditors in the property, but he could not appropriate the entire amount to the payment of his own debt. This, however, conferred no right upon appellants to seize the property, and sell it in satisfaction of the debt of Blatchford & Co. As creditors of the corporation they occupied no better position than Miller. It may be, and no doubt is, true, that if Blatchford & Co. had levied on the property while in the hands of the corporation, before the sale to Miller, they would, under such circumstances, have been entitled to hold it. But after the sale and delivery to Miller they had no such right,—the property had passed beyond the reach of their execution. It had passed into Miller's hands charged with a trust which a court of equity might enforce in favor of all the creditors of the corporation, or such as might invoke the aid of that court.*

NAPPANEE CANNING CO. v. REID, MURDOCH & CO.

1902. 159 Ind. 614, 64 N. E. 370.*

ACTION by Reid, Murdoch & Co. and others against the Nappanee Canning Company and others for damages for breach of an alleged contract, and to set aside, as fraudulent, a mortgage or deed of trust. From a judgment for plaintiffs, defendants appeal. Transferred from Appellate Court, under subdivision two of Sec. 1337j Burns 1901.

DOWLING, C. J.—In deciding the question before us, it is to be borne in mind that a manufacturing corporation, under the statutes of this State, is strictly a private association, organized and con-

* *Montgomery v. Phillips* (1895) 53 N. J. Eq. 203, 31 Atl. 622; *Slack v. N. W. Nat'l Bk.* (1899) 103 Wis. 57, 79 N. W. 51, 74 Am. St. 841; *Richards v. Holiday* (1899) 92 Fed. 798 *Accord*.

Cf. *In re Wincham Shipbuilding etc. Co.* (1878) L. R. 9 Ch. Div. 322; *Atlas Tack Co. v. Macon Hardware Co.* (1877) 101 Ga. 391, 29 S. E. 27; *Vanderpoel v. Goman* (1894) 140 N. Y. 563, 35 N. E. 932, 24 L. R. A. 548, 37 Am. St. 601; *Converse v. Sharpe* (1900) 161 N. Y. 571, 56 N. E. 69; *Sanford Fork & Tool Co. v. Howe, Brown & Co. Ltd.*, (1894) 157 U. S., 312, 39 L. ed. 713, 5 Sup. Ct. 621; *Sutton Mfg. Co. v. Hutchison* (1894) 63 Fed. 496, 11 C. C. A. 320. See 22 L. R. A. 817, note.—Eds.

* Portion of opinion omitted.—Eds.

ducted for private purposes only, enjoying no special privileges, and owing no duty to the public or to its creditors except such as is imposed by the terms of the statute under which it is formed, and by those general rules which apply to individuals engaged in business. Until its property passes into the custody of the law by seizure under proceedings in attachment, or by the appointment of an assignee, trustee, or receiver, the corporation may sell, transfer, pledge, or mortgage its property in the same manner and subject to the same restrictions only as apply to the case of a private person. Such property is in no respect held in trust for the creditors of the association. The law of this state gives them no lien or claim upon such property. They have no right to look to the corporation or its directors to protect their interests. They deal with it at arm's length, and their attitude is antagonistic to the association. When asked to extend credit to it, all persons dealing with the corporation know that if it is, or thereafter becomes, insolvent, the whole of its property may be applied to pay or secure debts due to favored creditors, including officers and directors, and that the claims of all other creditors may be excluded and consequently lost. If, with this knowledge, credit is given, it cannot be said that preferences subsequently conferred upon other creditors have violated any right which the law gave to the creditor whose claim was left unpaid and unsecured.

No statute gives to a creditor the right to demand an equal distribution of the assets of an insolvent private manufacturing corporation among its creditors. The maxim that, in case of insolvency, equality is equity has not the force of a statute requiring such a distribution. It is applicable only when the principles of equity are brought to bear upon the distribution of property lawfully in the custody of a court, where such court possesses the authority to make distribution upon that basis. The directors of a manufacturing corporation are not the agents or trustees of the creditors, but are simply and solely the representatives of the stockholders and of the corporation. There is no sufficient legal reason why they should be denied the right of preference in the event that the corporation becomes insolvent. And even if the vote of the director himself is necessary to authorize the execution of the instrument creating the preference, no legal wrong is done to the other creditors where such preference is given. The association is a legal entity distinct from the stockholders and from the directors. The action of the directors is their action, and not their individual act. The vote of a majority is required to pass any resolution or order, but the action of such majority is not necessarily vitiated by the fact that one or more of the persons composing it is interested in the passage of the resolution. The duty of the directors is to the corporation and its stockholders, not to the creditors. If the corporation or its stockholders acquiesce in the disposition of the corporate assets made by the directors, and if such disposition is the payment of a just debt owing

by the corporation, no matter to whom, it is difficult to perceive upon what legal ground a creditor can call such act in question. When it is understood that no trust exists in favor of creditors, that the directors are the agents of the stockholders and of the corporation only, and that they owe no special duty to the creditors of the company, it seems plain that, where the right to give preferences is recognized, the directors of an insolvent corporation may secure a *bona fide* debt owing to one of their own number.

As we have stated, it is established law in this State that an insolvent corporation may give preferences to the same extent and in like manner as an individual. In such transactions the corporation and its stockholders are the principal, the directors are their agents. If the vote of the director whose debt is secured is necessary to pass the resolution creating the preference, the only persons sustaining such relations to him as authorize them to object to his act are the stockholders and the corporation itself. The general rules governing the rights and duties of principal and agent apply in cases of this kind. The agent of a private person authorized to sell property may sell and convey to himself. Such sale is voidable but not void. If his principal does not object within a reasonable time, or with full knowledge ratifies the sale, it will stand. We have been referred to no case in which it has been held that where such sale is made in good faith, and for a fair and sufficient consideration, the creditors of the principal can avoid it on the ground of a violation of duty by the agent. *Fountain Coal Co. v. Phelps*, 95 Ind. 271; *Marsh v. Whitmore*, 21 Wall. (U. S.) 178, 22 L. ed. 482; *Eastern Bank v. Taylor*, 41 Ala. 93, 100.

The rule is that where the principal affirms the act of an agent a stranger will not be permitted to controvert it. *Scott v. Detroit, etc., Soc.*, 1 Doug. (Mich.) 119. "As the principal or parties interested may confirm the sale, a 'mere stranger' cannot make the objection that the trustee was the purchaser; or that the sale was irregular." *Dillon, J.*, in *Buell v. Buckingham and Co.*, 16 Iowa 284, 85 Am. Dec. 516.

Two of the special findings of fact are in these words: "That the said directors were sureties or otherwise legally bound on all the indebtedness of the said Canning Company, and, desiring to secure themselves from such liability, they caused said Canning Company, at a meeting called for that purpose, to execute the following instrument in writing, to wit: (Here follows the mortgage or deed of trust to Mosiman.) That the claims mentioned in said trust deed were just and *bona fide* debts of said Canning Company, and said trust deed was executed by authority of the entire board of directors of the said Canning Company."

Did the fact that the directors were sureties or otherwise legally bound for their payment, put it out of the power of the board of directors to secure the payment of these debts? The later and better authorities require us to answer this question in the negative. It

was said in *Levering v. Bimel*, 146 Ind. 545, that the effect of the decisions referred to in the opinion was that an insolvent corporation is not to be denied the right to prefer a creditor or creditors, even where such preference inures to the benefit of its officers who are sureties upon the claims of the creditors preferred. And the court further declared that the broad doctrine that the officers of a corporation cannot contract with it in their own names is unreasonable, and that the fact that the officer of a corporation would be able by reason of his position to outstrip the other creditors in the race of diligence in collecting or securing the claims upon which they were liable was not sufficient to deprive the corporation of the right to prefer such claims.

The courts holding that an interested director cannot vote, or even be counted for the purpose of making a quorum, seem to have proceeded entirely upon the theory that the director was a trustee for or an agent of the creditors, and therefore could not be permitted to advance his own interests at the expense of his principal or the cestui que trust. The directors are the agents and trustees of the corporation and its stockholders. As a director of an insolvent corporation is not a trustee for its creditors, and owes them no duty, where the debt to which preference is given is an honest and just debt of the corporation, the circumstance that the director is incidentally benefited by such preference, does not, in our opinion, absolutely disqualify him to take part in the proceedings of the directors, or to vote upon the proposition to secure such debt. If the corporation and the stockholders acquiesce in the action of the director creditor, outside creditors, who are strangers to the corporation, and have no lien or claim upon its property, cannot impeach the transaction. (The learned judge, after referring to numerous authorities, proceeded:)

Our conclusion, therefore, upon the reasons and authorities herein set out, is that the deed of trust executed by the Nappanee Canning Company to Mosiman, as trustee, to secure, among others, debts for which the directors of that company were liable, was valid, and enforceable against the property described in it.⁷

¹ *Corey v. Wadsworth*, et al (1897) 118 Ala. 488, 25 So. 503, 44 L. R. A. 766; *Bank of Montreal v. Potts Salt & Lumber Co.* (1892) 90 Mich. 345, 51 N. W. 512; *Butler v. Land & Mining Co.* (1897) 139 Mo. 467; *Planters' Bank of Farmville v. Whittle* (1884) 78 Va. 737; *South Bend Chilled Plow Co. v. George C. Cribb Co.* (1897) 97 Wis. 230, 72 N. W. 749, *Accord.*—Eds.

B—BY STATUTE. STATUTORY LIABILITY OF DIRECTORS TO CREDITORS.

HUNTINGTON v. ATTRILL.

1892. 146 U. S. 657, 36 L. ed. 1123.*

IN EQUITY. The bill was dismissed by the Court of Appeals of Maryland, to which judgment this writ of error was sued out.

GRAY, J.—This was a bill in equity, filed March 21, 1888, in the Circuit Court of Baltimore City, by Collis P. Huntington, a resident of New York, against the Equitable Gas Light Company of Baltimore, a corporation of Maryland, and against Henry Y. Attrill, his wife and three daughters, all residents of Canada, to set aside a transfer of stock in that company, made by him for their benefit and in fraud of his creditors, and to charge that stock with the payment of a judgment recovered by the plaintiff against him in the State of New York, upon his liability as a director in a New York corporation, under the statute of New York of 1875, c. 611, the material provisions of which are copied in the margin.^a

The bill alleged that on June 15, 1886, the plaintiff recovered, in the Supreme Court of the State of New York, in an action brought by him against Attrill on March 21, 1883, a judgment for the sum of \$100,240, which had not been paid, secured or satisfied; and that the cause of action on which that judgment was recovered was as follows: On February 29, 1880, the Rockaway Beach Improvement Company, Limited, of which Attrill was an incorporator and a director, became a corporation under the law of New

* Portions of the opinion omitted.—Eds.

^a SEC. 21. If any certificate or report made, or public notice given, by the officers of any such corporation, shall be false in any material representation, all the officers who shall have signed the same shall be jointly and severally liable for all the debts of the corporation contracted while they are officers thereof.

SEC. 37. In limited liability companies, all the stockholders shall be severally individually liable to the creditors of the company in which they are stockholders, to an amount equal to the amount of stock held by them respectively, for all debts and contracts made by such company, until the whole amount of capital stock fixed and limited by such company has been paid in, and a certificate thereof has been made and recorded as hereinafter prescribed. . . . The capital stock of every such limited liability company shall be paid in, one-half thereof within one year and the other half thereof within two years from the incorporation of said company, or such corporation shall be dissolved. The directors of every such company, within thirty days after the payment of the last instalment of the capital stock, shall make a certificate stating the amount of the capital so paid in, which certificate shall be signed and sworn to by the president and a majority of the directors; and they shall, within the said thirty days, record the same in the office of the secretary of state, and of the county in which the principal business office of such corporation is situated.

SEC. 38. The dissolution for any cause whatever, of any corporation created as aforesaid, shall not take away or impair any remedy given against such corporation, its stockholders or officers, for any liabilities incurred previous to its dissolution.

York, with a capital stock of \$700,000. On June 15, 1880, the plaintiff lent that company the sum of \$100,000, to be repaid on demand. On February 26, 1880, Attrill was elected one of the directors of the company, and accepted the office, and continued to act as a director until after January 29, 1881. On June 30, 1880, Attrill, as a director of the company, signed and made oath to and caused to be recorded, as required by the law of New York, a certificate, which he knew to be false, stating that the whole of the capital stock of the corporation had been paid in, whereas in truth no part had been paid in; and by making such false certificate became liable by the law of New York, for all the debts of the company contracted before January 29, 1881, including its debt to the plaintiff. On March 8, 1882, by proceedings in a court of New York, the corporation was declared to be insolvent and to have been so since July, 1880, and was dissolved. A duly exemplified copy of the record of that judgment was annexed to and made part of the bill. * * *

It thus appears that the judgment recovered in New York was made the foremost ground of the bill, was fully discussed and distinctly passed upon by the majority of the Court of Appeals of Maryland, and was the only subject of the dissenting opinion; and that the court, without considering whether the validity of the transfers impeached as fraudulent was to be governed by the law of New York or by the law of Maryland, and without a suggestion that those transfers, alleged to have been made by Attrill with intent to delay, hinder and defraud all his creditors, were not voidable by subsequent, as well as by existing creditors, or that they could not be avoided by the plaintiff, claiming under the judgment recovered by him against Attrill after those transfers were made, declined to maintain his right to do so by virtue of that judgment, simply because the judgment had, as the court held, been recovered in another State in an action for a penalty.

The question whether due faith and credit were thereby denied to the judgment rendered in another State is a Federal question, of which this court has jurisdiction on this writ of error. *Green v. Van Buskirk*, 5 Wall. 307, 311; *Crapo v. Kelly*, 16 Wall. 610, 619; *Dupasseur v. Rochereau*, 21 Wall. 130, 134; *Crescent City Co. v. Butchers' Union*, 120 U. S. 141, 146, 147; *Cole v. Cunningham*, 133 U. S. 107; *Carpenter v. Strange*, 141 U. S. 87, 103.

In order to determine this question, it will be necessary, in the first place, to consider the true scope and meaning of the fundamental maxim of international law, stated by Marshall, Ch. J., in the fewest possible words: "The courts of no country execute the penal laws of another." *The Antelope*, 10 Wheat. 66, 123. In interpreting this maxim, there is danger of being misled by the different shades of meaning allowed to the word "penal" in our language.

In the municipal law of England and America, the words "penal" and "penalty" have been used in various senses. Strictly

and primarily, they denote punishment, whether corporal or pecuniary, imposed and enforced by the State, for a crime or offense against its laws. *United States v. Reisinger*, 128 U. S. 398, 402; *United States v. Chouteau*, 102 U. S. 603, 611. But they are also commonly used as including any extraordinary liability to which the law subjects a wrongdoer in favor of the person wronged, not limited to the damages suffered. They are so elastic in meaning as even to be familiarly applied to cases of private contracts, wholly independent of the statutes, as when we speak of the "penal sum" or "penalty" of a bond. In the words of Marshall, Ch. J.: "In general, a sum of money in gross, to be paid for the non-performance of an agreement, is considered as a penalty, the legal operation of which is to cover the damages which the party, in whose favor the stipulation is made, may have sustained from the breach of contract by the opposite party." *Tayloe v. Sandiford*, 7 Wheat. 13, 17.

Penal laws, strictly and properly, are those imposing punishment for an offense committed against the State, and which, by the English and American Constitutions, the executive of the State has the power to pardon. Statutes giving a private action against the wrongdoer are sometimes spoken of as penal in their nature, but in such cases it has been pointed out that neither the liability imposed nor the remedy given is strictly penal. * * *

The test whether a law is penal, in the strict and primary sense, is whether the wrong sought to be redressed is a wrong to the public, or a wrong to the individual, according to the familiar classification of Blackstone: "Wrongs are divisible into two sorts or species: private wrongs and public wrongs. The former are an infringement or privation of the private or civil rights belonging to individuals, considered as individuals; and are thereupon frequently termed civil injuries; the latter are a breach and violation of public rights and duties, which affect the whole community, considered as a community; and are distinguished by the harsher appellation of crimes and misdemeanors." 3 Bl. Com. 2.

Laws have no force of themselves beyond the jurisdiction of the State which enacts them, and can have extra-territorial effect only by the comity of other States. The general rules of international comity upon this subject were well summed up, before the American Revolution, by De Grey, Ch. J., as reported by Sir William Blackstone: "Crimes are in their nature local, and the jurisdiction of crimes is local. And so as to the rights of real property, the subject being fixed and immovable. But personal injuries are of a transitory nature, and *sequuntur forum rei*." *Rafael v. Verelst*, 2 W. Bl. 1055, 1058.

Crimes and offenses against the laws of any State can only be defined, prosecuted and pardoned by the sovereign authority of that State; and the authorities, legislative, executive or judicial, of other States take no action with regard to them, except by way of extradi-

tion to surrender offenders to the State whose laws they have violated, and whose peace they have broken. * * *

The question whether a statute of one State, which in some aspects may be called penal, is a penal law in the international sense, so that it cannot be enforced in the courts of another State, depends upon the question whether its purpose is to punish an offense against the public justice of the State, or to afford a private remedy to a person injured by the wrongful act. * * *

The provision of the statute of New York, now in question, making the officers of a corporation, who sign and record a false certificate of the amount of its capital stock, liable for all its debts, is in no sense a criminal or quasi criminal law. The statute, while it enables persons complying with its provisions to do business as a corporation, without being subject to the liability of general partners, takes pains to secure and maintain a proper corporate fund for the payment of the corporate debts. With this aim, it makes the stockholders individually liable for the debts of the corporation until the capital stock is paid in and a certificate of the payment made by the officers; and makes the officers liable for any false and material representation in that certificate. The individual liability of the stockholders takes the place of a corporate fund, until that fund has been duly created; and the individual liability of the officers takes the place of the fund, in case their statement that it has been duly created is false. If the officers do not truly state and record the facts which exempt them from liability, they are made liable directly to every creditor of the company, who by reason of their wrongful acts has not the security, for the payment of his debt out of the corporate property, on which he had a right to rely. As the statute imposes a burdensome liability on the officers for their wrongful act, it may well be considered penal, in the sense that it should be strictly construed. But as it gives a civil remedy, at the private suit of the creditor only, and measured by the amount of his debt, it is as to him clearly remedial. To maintain such a suit is not to administer a punishment imposed upon an offender against the State, but simply to enforce a private right secured under its laws to an individual. We can see no just ground, on principle, for holding such a statute to be a penal law, in the sense that it cannot be enforced in a foreign state or country.

The decisions of the Court of Appeals of New York, so far as they have been brought to our notice, fall short of holding that the liability imposed upon the officers of the corporation by such statutes is a punishment or penalty which cannot be enforced in another State.

In *Garrison v. Howe*, the court held that the statute was so far penal that it must be construed strictly, and therefore the officers could not be charged with a debt of the corporation, which was neither contracted nor existing during a default in making the report required by the statute; and Chief Justice Denio, in delivering judg-

ment, said: "If the statute were simply a remedial one, it might be said that the plaintiff's case was within its equity; for the general object of the law doubtless was, beside enforcing the duty of making reports for the benefit of all concerned, to enable parties proposing to deal with the corporation to see whether they could safely do so." "But the provision is highly penal, and the rules of law do not permit us to extend it by construction to cases not fairly within the language." 17 N. Y. 458, 465, 466.

In *Jones v. Barlow*, it was accordingly held that officers were only liable for debts actually due, and for which a present right of action exists against the corporation; and the court said: "Although the obligation is wholly statutory, and adjudged to be a penalty, it is in substance, as it is in form, a remedy for the collection of the corporate debts. The act is penal as against the defaulting trustees, but is remedial in favor of creditors. The liability of defaulting trustees is measured by the obligation of the company, and a discharge of the obligations of the company, or a release of the debt, bars the action against the trustees." 62 N. Y. 202, 205, 206.

The other cases in that court, cited in the opinion of the Court of Appeals of Maryland in the present case, adjudged only the following points: Within the meaning of a statute of limitations applicable to private actions only, the action against an officer is not "upon a liability created by statute, other than a penalty or forfeiture," which would be barred in six years, but is barred in three years as "an action upon a statute for a penalty or forfeiture where action is given to the party aggrieved," because the provisions in question, said the court, "impose a penalty, or a liability in that nature." *Merchants' Bank v. Bliss*, 35 N. Y. 412, 417. A count against a person as an officer for not filing a report cannot be joined with one against him as a stockholder for debts contracted before a report is filed, that being "an action on contract." *Wiles v. Suydam*, 64 N. Y. 173, 176. The action against an officer is an action *ex delicto*, and therefore does not survive against his personal representatives. *Stokes v. Stickney*, 96 N. Y. 323.

In a later case than any of these, the court, in affirming the very judgment now sued on, and adjudging the statute of 1875 to be constitutional and valid, said that "while liability within the provision in question is in some sense penal in its character, it may have been intended for the protection of creditors of corporations created pursuant to that statute." *Huntington v. Attrill*, 118 N. Y. 365, 378. And where such an action against an officer went to judgment before the death of either party, it was decided that "the original wrong was merged in the judgment, and that thus became property with all the attributes of a judgment in an action *ex contractu*," and that if, after a reversal of judgment for the plaintiff, both parties died, the plaintiff's representatives might maintain an appeal from the judgment of reversal, and have the defendant's representatives summoned in. *Carr v. Rischer*, 119 N. Y. 117, 124.

We do not refer to these decisions as evidence in this case of the law of New York, because in the courts of Maryland that law could only be proved as a fact, and was hardly open to proof on the demurrer, and, if not proved in those courts, could not be taken judicial notice of by this court on this writ of error. *Hanley v. Donoghue*, 116 U. S. 1; *Chicago & Alton Railroad v. Wiggins Ferry*, 119 U. S. 615; *Wernwag v. Pawling*, 5 Gill & Johns. 500, 508; *Coates v. Mackey*, 56 Maryland, 416, 419. Nor, for reasons to be stated presently, could those decisions, in any view, be regarded as concluding the courts of Maryland, or this court, upon the question whether this statute is a penal law in the international sense. But they are entitled to great consideration, because made by a court of high authority, construing the terms of a statute with which it was peculiarly familiar; and it is satisfactory to find no adjudication of that court inconsistent with the view which we take of the liability in question.

That court and some others, indeed, have held that the liability of officers under such a statute is so far in the nature of a penalty, that the creditors of the corporation have no vested right therein, which cannot be taken away by a repeal of the statute before judgment in an action brought thereon. *Victory Co. v. Beecher*, 97 N. Y. 651, and 26 Hun, 48; *Union Iron Co. v. Pierce*, 4 Bissell, 327; *Breitung v. Lindauer*, 37 Michigan, 217, 230; *Gregory v. German Bank*, 3 Colorado, 332. But whether that is so; or whether, within the decision of this court in *Hawthorne v. Calef*, 2 Wall. 10, 23, such a repeal so affects the security which the creditor had when his debt was contracted, as to impair the obligation of his contract with the corporation, is aside from the question now before us.

It is true that the courts of some States, including Maryland, have declined to enforce a similar liability imposed by the statute of another State. But, in each of those cases, it appears to have been assumed to be a sufficient ground for that conclusion, that the liability was not founded in contract, but was in the nature of a penalty imposed by statute; and no reasons were given for considering the statute a penal law in the strict, primary and international sense. *Derrickson v. Smith*, 3 Dutcher (27 N. J. Law), 166; *Halsey v. McLean*, 12 Allen, 438; *First National Bank v. Price*, 33 Maryland, 487.

It is also true that in *Steam Engine Co. v. Hubbard*, 101 U. S. 188, 192, Mr. Justice Clifford referred to those cases by way of argument. But in that case, as well as in *Chase v. Curtis*, 113 U. S. 452, the only point adjudged was that such statutes were so far penal that they must be construed strictly; and in both cases jurisdiction was assumed by the Circuit Court of the United States, and not doubted by this court, which could hardly have been if the statute had been deemed penal within the maxim of international law. In *Flash v. Conn*, 109 U. S. 371, the liability sought to be enforced under the statute of New York was the liability of a stockholder aris-

ing upon contract; and no question was presented as to the nature of the liability of officers.

But in *Hornor v. Henning*, 93 U. S. 228, this court declined to consider a similar liability of officers of a corporation in the District of Columbia as a penalty. See also *Neal v. Moultrie*, 12 Georgia, 104; *Cady v. Sanford*, 53 Vermont, 632, 639, 640; *Nickerson v. Wheeler*, 118 Mass. 295, 298; *Post v. Toledo &c. Railroad*, 144 Mass. 341, 345; *Woolverton v. Taylor*, 132 Illinois, 197; *Morawetz on Corporations* (2d ed.) § 908. * * *

The judgment rendered by a court of the State of New York, now in question, is not impugned for any want of jurisdiction in that court. The statute under which that judgment was recovered was not, for the reasons already stated at length, a penal law in the international sense. The faith and credit, force and effect, which that judgment had by law and usage in New York was to be conclusive evidence of a direct civil liability from the individual defendant to the individual plaintiff for a certain sum of money, and a debt of record, on which an action would lie as on any other civil judgment inter partes. The Court of Appeals of Maryland, therefore, in deciding this case against the plaintiff, upon the ground that the judgment was not one which it was bound in any manner to enforce, denied to the judgment the full faith, credit and effect to which it was entitled under the Constitution and laws of the United States.

Judgment *reversed*, and case remanded to the Court of Appeals of the State of Maryland for further proceedings not inconsistent with the opinion of this court.*

* See *National Bank of Auburn v. Dillingham* (1895) 147 N. Y. 603, 42 N. E. 388, 49 Am. St. 692; *Hutchinson v. Stadler* (1903) 85 App. Div. (N. Y.) 424, 83 N. Y. S. 509; *Davey v. Brooklyn & N. Y. Ferry Co.*, 196 N. Y. 99.

In *Hutchinson v. Young* (1903) 80 App. Div. (N. Y.) 246, 80 N. Y. S. 259, *Held*, that an action under sec. 31 of the N. Y. Stock Corporation Law (Laws of 1890, ch. 564, as amended by ch. 688, Laws of 1892) providing for the liability on account of a false report to the extent of the damages sustained by the person acting in reliance thereon, is not an action covered by sec. 983 of the Code of Civil Procedure relating to actions "to recover a penalty or forfeiture imposed by statute."

In *Hutchinson v. Young* (1904) 93 App. Div. (N. Y.) 407, 87 N. Y. S. 678; *Held*, that an action under sec. 31 of the N. Y. Corporation Law may be joined in the same complaint with a common-law action for deceit, both actions being *ex delicto*.

In *Yates v. Jones Nat. Bk.* (1906) 206 U. S. 158, 51 L. ed. 1002, 27 Sup. Ct. 638, *Held*, that where a statute imposes a duty upon a director and prescribes a penalty for its non-performance, the rule prescribed by the statute is the exclusive test of liability and of the standard of conduct required.—Eds.

Section 3.—Relation Between Creditor and Stockholder.**A. AT COMMON LAW. THE TRUST FUND THEORY.****(1) *Rights of Creditors with Respect to Unpaid Subscriptions.*****HATCH v. DANA.**1879. 101 U. S. 205, 25 L. ed. 885.¹

APPEAL from the Circuit Court of the United States for the Southern District of Illinois.

On April 12, 1871, Charles A. Dana recovered a judgment in the Circuit Court of the United States for the Northern District of Illinois against the Chicago Republican Co., a corporation organized and existing under the laws of the State of Illinois, for the sum of \$6419.17 and costs.

An execution issued upon this judgment was by the marshal of the United States for that district returned *nulla bona*.

Thereupon, on August 23, 1871, Dana, on behalf of himself and all other creditors of the company who might come in and seek relief by and contribute to the expense of the suit, exhibited in the Circuit Court of the United States for the Southern District of Illinois his bill in equity against the company, Hatch, Williams and other resident stockholders, averring the incorporation of the company in February, 1865, with a capital stock of \$500,000, divided into shares of \$100 each; that at a meeting of the incorporators, held in Chicago in April, 1865, certain stock subscriptions were made, Hatch and Williams each subscribing for one hundred shares; that a complete organization of the company was effected, and an assessment of twenty per cent. declared upon the stock subscribed, the company thereupon commencing business; that eighty per cent. of the subscriptions to stock so made still remains unpaid; that in October, 1870, the company so organized sold and transferred all its tangible property, credits, and subscription lists to a corporation of a very similar name, and thereupon ceased to do business; that the company is wholly insolvent; avers the recovery of the judgment aforesaid, the issue and the return unsatisfied of an execution thereon; that there are no other unpaid creditors than the complainant. It prays that, upon an accounting of the amount unpaid upon the stock subscriptions of the stockholders named as defendants, they may be decreed to pay so much of the balance found unpaid on their respective subscriptions as will be sufficient to pay the ascertained debts of the corporation, including the judgment aforesaid; and for general relief.

The complainant dismissed the bill as to all of the defendants, except Hatch and Williams. * * *

¹ Portion of statement of facts and opinion omitted.—Eds.

The facts of the case are set out in the complainant's bill. A decree was rendered January 6, 1879, that the complainant, Charles A. Dana, recover of Hatch and Williams the sum of \$9398.72, being the amount due on that day upon the said judgment, and that they pay the costs of the suit to be taxed, it being provided, however, that of the sum so decreed to be paid not more than \$7000, together with interest thereon from the date of the decree, at the rate of six per cent. per annum, shall be made and collected from either said Hatch or Williams, the said sum of \$7000 being the amount the court finds each of them to owe and be indebted to the Chicago Republican Co.

From this decree Hatch and Williams appealed.

STRONG, J.—This bill is an ordinary creditor's bill, the sole object of which is to obtain payment of the complainant's judgment. It is true it is brought on behalf of the complainant and all other creditors of the corporation who might choose to come in and seek relief by it, contributing to the expense of the suit. But no other creditors came in; and it does not appear that there is any other creditor, unless it be one of the stockholders, who was made a defendant, and who filed a cross-bill which he afterward dismissed. All the stockholders were not made defendants.

The bill was not a bill seeking to wind up the company. It sought simply payment of a debt out of the unpaid stock subscriptions.

That unpaid stock subscriptions are to be regarded as a fund, which the corporation holds for the payment of its debts, is an undeniable proposition. But the appellants insist that a creditor of an insolvent corporation is not at liberty to proceed against one or more delinquent subscribers to recover the amount of his debt without an account being taken of other indebtedness, and without bringing in all the stockholders for contribution. They insist also that by the terms of the subscriptions for stock made by these appellants they were to pay for the shares set opposite their names respectively, "as called for by the said company;" that the company made no calls for more than thirty per cent.; that, therefore, this company could not recover the seventy per cent. unpaid without making a previous call; and that a court of equity will not enforce the contract differently from what was contemplated in the subscription.

These positions, we think, are not supported by the authorities—certainly not by the more modern ones—nor are they in harmony with sound reason when considered with reference to the facts of this case. The liability of a subscriber for the capital stock of a company is several, and not joint. By his subscription each becomes a several debtor to the company, as much so as if he had given his promissory note for the amount of his subscription. At law, certainly, his subscription may be enforced against him without joinder of other subscribers; and in equity his liability does not cease to be several. A creditor's bill merely subrogates the creditor to the place of the debtor, and garnishes the debt due to the indebted corporation. It does not change the character of the debt attached or gar-

nished. It may be that if the object of the bill is to wind up the affairs of this corporation, all the shareholders, at least so far as they can be ascertained, should be made parties, that complete justice may be done by equalizing the burdens, and in order to prevent a multiplicity of suits. But this is no such case. The most that can be said is that the presence of all the stockholders might be convenient, not that it is necessary. When the only object of a bill is to obtain payment of a judgment against a corporation out of its credits or intangible property—that is, out of its unpaid stock, there is not the same reason for requiring all the stockholders to be made defendants. In such a case no stockholder can be compelled to pay more than he owes.

In *Ogilvie v. Knox Insurance Co.*, 22 How. 380, the question was considered. That was a case in which several judgment creditors of a corporation had brought a creditor's bill against it and thirty-six subscribers to its capital stock. The bill alleged that the complainants had recovered judgments against the company, upon which executions had been issued and returned "no property;" that the other defendants had severally subscribed for its stock, and that the subscriptions remained unpaid, payment not having been enforced by the company. The prayer of the bill was that these other defendants might be decreed to pay their subscriptions, and that the judgments might be satisfied out of the sum paid. It was objected, as here, that the bill was defective for want of proper parties; but the court held the objection untenable. In delivering the opinion of the court, Grier, J., said: "The creditors of the corporation are seeking satisfaction out of the assets of the company to which the defendants are debtors. If the debts attached are sufficient to pay their demands, the creditors need look no further. They are not bound to settle up all the affairs of this corporation, and the equities between its various stockholders, corporators, or debtors. If A is bound to pay his debt to the corporation in order to satisfy its creditors, he cannot defend himself by pleading that these complainants might have got their satisfaction out of B as well. It is true, if it be necessary to a complete satisfaction of the complainants that the corporation be treated as an insolvent, the court may appoint a receiver, with authority to collect and receive all the debts due to the company, and administer all its assets. In that way all the other stockholders or debtors may be made to contribute." The court, therefore, directed a decree against the respondents severally for such amounts as appeared to be due and unpaid by each of them for their shares of the capital stock.

This case is directly in point, and it does not stand alone. In *Bartlett v. Drew*, 57 N. Y. 587, it was ruled that when the property of a corporation had been divided among its stockholders before all its debts had been paid, a judgment creditor, after the return of an execution unsatisfied, might maintain an action, in the nature of a creditor's bill, against a stockholder to reach whatsoever was so re-

ceived by him, and that he was not required to make all the stockholders parties to the action; that he had nothing to do with the equities between the stockholders, unless he chose to intervene to settle them. This is much beyond what the complainant needs in this case. It is enforcing against stockholders in severalty what the corporation could not enforce, without any regard to the equities of one against the others. * * *

The cases of Pollard v. Bailey, 20 Wall. 520, and Terry v. Tubman, 92 U. S. 156, are not in conflict with Ogilvie v. Knox Insurance Co. They arose under statutory provisions imposing upon the stockholders of banks a liability for the debts of the corporation, "in proportion to their stock held therein." It was this liability beyond the stock subscription which was sought to be enforced, and as it was only a proportional liability, its extent could be ascertained only when the obligation of the other shareholders was taken into consideration. Hence it was ruled that the proper mode of proceeding was by bill in equity in which an account of the debts and stock could be taken and a *pro rata* distribution could be made. Not a hint was given that the latter case was intended to be questioned or qualified. Indeed, Pollard v. Bailey and Terry v. Tubman have little analogy to it or to the case we have now before us. They were both suits at law. The debt due by these appellants to the corporation of which they are members is a fixed and definite one, and it is neither more nor less because other debts may be due to the company from other stockholders.

We hold, therefore, that the complainant was under no obligation to make all the stockholders of the bank defendants in his bill. It was not his duty to marshal the assets of the bank or to adjust the equities between the corporators. In all that he had no interest. The appellants may have had such an interest, and if so, it was quite in their power to secure its protection. They might have moved for a receiver, or they might have filed a cross-bill, obtained a discovery of the other stockholders, brought them in, and enforced contribution from all who had not paid their stock subscriptions. Their equitable right to contribution is not yet lost.

That the appellants are not protected by the fact, if such was the fact, that their subscriptions for stock were payable "as called for by the company," we think is clear. Assuming that such a clause in the subscription meant more than an agreement to pay on demand, and that it contemplated a formal call upon all subscribers to the stock of the company, the subscriptions were still in the nature of a fund for the payment of the company's debts, and it was the duty of the company to make the calls whenever the funds were needed for such payment. If they were not made, the officers of the company violated their trust, held both for the stockholders and the company. And it would seem to be singular if the stockholders could protect themselves from paying what they owe by setting up the default of their own agents. But in this case the company went out of busi-

ness before the complainant obtained his judgment, and it does not appear that since that time it has had any officers who could make the calls. Before that time its president was dead. However this may be, it is well settled that a court of equity may enforce the payment of stock subscriptions though there have been no calls for them by the company. In *Henry v. Railroad Co.*, 17 Ohio, 187, a suit brought by a judgment creditor of a corporation to enforce payment by its stockholders of their unpaid subscriptions, for which calls had not been made, it was held that when a company ceases to keep up its organization, and abandons all action under the charter, a proceeding at the instance of the creditor becomes indispensable. It was further said: "When a company, becoming insolvent, as in this case, abandons all action under its charter, the original mode of making calls upon the stockholders cannot be pursued. The debt, therefore, from that time must be treated as due without further demand." This means, of course, as between the debtor and the creditor of the corporation. After all, a company call is but a step in the process of collection, and a court of equity may pursue its own mode of collection, so that no injustice is done to the debtor.

In the English courts a mandamus is sometimes awarded to compel the directors to make the necessary calls. *Queen v. The Victoria Park Co.*, 1 Ad. & El. (N. S.) 544; *Queen v. Ledgard*, id. 616; *The King v. Katharine Dock Co.*, 4 Barn. & Ad. 360. But this remedy can avail only when there are directors. The remedy in equity is more complete, and it is well recognized. *Ward v. The Griswoldville Manufacturing Co.*, 16 Conn. 593. In such cases it is nowhere held, so far as we know, that a formal call must be made before a bill can be filed. Indeed, the filing of the bill is equivalent to a call. Before it is filed the court has no jurisdiction of the matter. In bankruptcy, an assessment or a call may be made, for the assignee of a bankrupt corporation succeeds to its rights and becomes the legal owner. Not so in equity.

In the *Dalton, etc., Railroad Co. v. McDaniel*, 56 Ga. 191, a creditor's bill very like the present was filed. It was objected by the stockholders, who were defendants, that it was for the directors of the company and not for the court to call in the stock subscriptions, and that their contract only obligated them to obey a call emanating from the company; but it was ruled that "principle and sound reason accord with authority that equity will grant relief in all such cases."

In view of these considerations we think none of the assignments of error is sustained.

*Decree affirmed.*²

² See *Gainey v. Gilson, Receiver* (1897) 149 Ind. 58, 48 N. E. 633; *Marion Trust Co., Receiver, v. Blish*, (1908) 170 Ind. 686, 84 N. E. 814, 85 N. E. 344, 18 L. R. A. (N. S.) 347n; *Shields v. Hobart*, (1902) 172 Mo. 491, 72 S. W. 675; *Stoddard v. Lum* (1899) 159 N. Y. 265, at page 275, 53 N. E. 1108, 45 L. R. A. 551, 70 Am. St. 541: "A subscription to the stock of a corporation creates a debt enforceable at law, or in equity, by the corporation, or its legal representative".—Eds.

HOWARD, RECEIVER v. TURNER

1893. 155 Pa. St. 349, 26 Atl. 753.*

Opinion by Mr. CHIEF JUSTICE STERRETT.—

(The learned judge, after summarizing the evidence in the case, proceeded:)

The foregoing are the salient facts, as to the origin, consideration, etc., of the note in suit, leading up to the defense that was successfully interposed in the court below, viz.: that the agreement to take the stock, giving the original note in payment thereof, etc., was induced by the fraudulent misrepresentations of the cashier as agent of the bank in procuring subscriptions, etc.

Without referring to the alleged misrepresentations, but assuming, for argument's sake merely, that they were such as would have justified the defendant in rescinding the contract before the bank became insolvent or other rights attached, the controlling question, under all the evidence, is whether that defense was available at the time it was interposed.

As a general rule, it is well settled that a contract induced by fraud is not void, but voidable only at the option of the party defrauded. In other words, it is valid until rescinded, and it is for the defrauded party to elect whether he will be bound; but, if he affirms the contract, he must affirm it in all its terms. Pollock, *Contracts*, 536; *Pearsoll v. Chapin*, 44 Pa. 9. When, however, the fraud is of such a character as to involve a crime, ratification thereof is contrary to public policy and cannot be permitted; but, where the transaction is merely contrary to good faith and fair dealing,—where it affects individual interests only—either ratification or rescission, at the election of the party defrauded, is permissible: *Shisler v. Vandike*, 92 Pa. 447; *Babcock v. Case*, 61 Pa. 431; *Leaming v. Wise*, 73 Pa. 173. In the last case it is said if defendants were guilty of the alleged fraud, the plaintiffs, on discovering it, had an undoubted right to rescind the contract, and upon a tender of the stocks to demand back the price paid for them, but it was their duty to do so within a reasonable time. Omission to repudiate within a reasonable time is evidence, and may be conclusive evidence of an election to affirm the contract. Election to rescind must be communicated to the other party. One way of doing that is to institute proceedings to have the contract judicially set aside; or, if the other party is the first to sue on the contract, the rescission, if not too late, may be set up as a defense. Where rescission is not declared in judicial proceedings, no further rule can be laid down than that there should be “prompt repudiation and restitution as far as possible.”

A contract, to take and pay for stock in a corporation, made in consequence of a fraudulent prospectus is voidable only and not void, and can only be avoided subject to the rights of creditors,

* Portion of the opinion omitted.—Eds.

where there is a winding up order or a voluntary winding up: Bispham's Equity, § 472; 2 Addison, Cont., 8th ed. 774; Cook on Stock, etc. §§ 151 to 154. The intervening rights of creditors and other stockholders call for prompt action on the part of a subscriber who seeks to avoid his liability on the ground of fraud; Bispham's Equity, sec. 154.

In view of these principles, and the uncontradicted facts above referred to, it is impossible to see any ground on which a valid defense in this case could be based. The undisputed evidence is that prior to the failure of the bank and institution of this suit by the receiver, neither the defendant nor his wife took any steps to rescind or repudiate the contract of subscription or to surrender the certificate of stock, as to which he testified, "It was left on the table; I suppose I accepted it;" nor did he deny his liability on the note. On the contrary, up to the time suit was brought, they both indicated a willingness to join with other shareholders in their efforts to reorganize the bank. Mrs. Turner, as we have seen, wrote to the chairman of the reorganization committee: "I want or expect to pay my 50 per cent. towards reorganizing the bank; but do not wish to send the amount until I know positively that you are going to reorganize," etc. A few days thereafter defendant wrote to the same effect, saying his wife would likely pay the assessment "should the bank be reorganized," but she did not want to borrow the money for that purpose "unless it is a sure go." At that time, as the chairman wrote them in reply, the whole amount of the assessment, \$100,000, except Mrs. Turner's and two others, was in, and one of those was on the way. Reorganization was then practically an accomplished fact. Everything, including the conduct of defendant and his wife, pointed to that conclusion; and doubtless the remittance would have been made if the receiver had not brought suit in the meantime. That, as Mrs. Turner wrote, "blocked matters for the present." In nothing that was said or done, from the beginning up to that time, was there anything that could be tortured into election to rescind on the part of the defendant. At that time, or rather prior thereto, the rights of the bank's creditors, to the extent of its assets, including the additional capital stock represented in part by defendant's note, had attached; the stockholders, with the exception of Mrs. Turner and one or two others, relying on obtaining possession of all the assets, had contributed nearly \$100,000 for the purpose of reorganizing the bank, which of course included settlement and payment of all its liabilities. These facts were established by uncontroverted evidence. There was no testimony from which any jury could, or ought to be permitted to find a state of facts more favorable to the defendant.*

* See *People v. Cal. Safe Deposit & Tr. Co.* (1912) (Cal.) 126 Pac. 516; *Ramsey v. Thompson Mfg. Co.* (1893) 116 Mo. 313, 22 S. W. 719; *Hillard v. Allegheny Geometrical Wood Carving Co.* (1895) 173 Pa. St. 1, 34 Atl. 231; *Scott v. Deweese* (1900) 181 U. S. 202, 45 L. ed. 822, 21 Sup. Ct. 585; *Lantrey*

(2) *Rights of Creditors Against Holders of Stock Issued for Money at Less Than Par.*

CHRISTENSEN v. ENO.

1887. 106 N. Y. 97, 12 N. E. 648.

APPEAL by defendant Eno from judgment of the General Term of the Supreme Court in the First Judicial Department, entered upon an order made January 21, 1885, which affirmed a judgment in favor of plaintiff, entered upon a decision of the court on trial at Special Term.

This action was brought by plaintiff, as judgment creditor of defendant, the Illinois & St. Louis Bridge Co., against it and defendant Eno, among other things, to compel the latter to pay forty per cent. of the par of twenty-five shares of the stock of said company issued by it to him, upon which stock the forty per cent. was not paid, but was credited as paid when the stock was issued; also, to compel said defendant to account for and pay over, in satisfaction of plaintiff's judgment, the proceeds of the sale by him of certain second mortgage bonds gratuitously issued to said Eno as a stockholder by said corporation, upon payment by him of the remaining sixty per cent. of said stock.

ANDREWS, J. The judgment below proceeds on the ground that the forty per cent. credited as paid on the twenty-five shares of stock of the Illinois & St. Louis Bridge Co., issued to the defendant Eno, in 1871, but which was not in fact paid, and also the sum of \$5332.18, realized by him on the sale of second mortgage bonds of the company, received as his share on the distribution of the same among stockholders, pursuant to the resolution of the company of December 20, 1871, were equitable assets in the hands of the defendant Eno, applicable to the payment of the debts of the corporation, and which the plaintiff, as a judgment and execution creditor, may reach in this action and have applied to the satisfaction of his judgment. It is very plain upon the facts, that the plaintiff in asserting this claim cannot stand upon any right existing in the corporation itself to proceed against the defendant Eno. The transactions by which he acquired the shares as paid-up shares to the extent of forty per cent. of their nominal amount, and received the bonds, created no obligation as between him and the

v. Wallace (1900) 182 U. S. 536, 45 L. ed. 1218, 21 Sup. Ct. 878; Brown v. Allebach (1908) 166 Fed. 488; note, 13 Col. Law Review, 62.

In Scott v. Deweese, 181 U. S., at page 213, 45 L. ed. 822, 828, 21 Sup. Ct. 585; the court said: "If the subscriber became a stockholder in consequence of frauds practised upon him by others, whether they be officers of the bank or officers of the Government, he must look to them for redress and is estopped as against creditors to deny that he is a shareholder, within the meaning of Section 5151, if at the time the rights of the creditors accrued, he occupied and was accorded the rights appertaining to that position".—Eds.

company to pay the amount unpaid on the stock or to account to the company for the bonds or their proceeds. As between Eno and the company it was not intended that the former should be accountable to the company for the amount unpaid on the stock or for the bonds. Viewing the transactions in the light most favorable to the plaintiff, the credit on the stock and the transfer of the bonds were intended as a gratuity to the stockholders who had been called upon to pay calls upon their original subscriptions in excess of what was expected and of what was represented would be necessary at the commencement of the enterprise. There can be no doubt that as between the corporation and its stockholders these transactions were binding according to the actual intention. The corporation itself would have no standing to demand that the defendant Eno should pay the forty per cent. on the stock which it acknowledged had been paid, or that he should account for the proceeds of the bonds. The claim of the plaintiff, therefore, must be maintained, if at all, not in right of the corporation, or by way of equitable subrogation to any right of the corporation against Eno, but in hostility to the arrangement between them, under which he received the stock and bonds. The plaintiff, to entitle himself to the relief demanded, is compelled to maintain that, as a creditor of the corporation, he has rights superior to those of the corporation itself and may hold the defendant to account for the unpaid forty per cent. on the stock as though he had been a subscriber therefor, and for the proceeds of the bonds as though he had purchased them of the corporation, or had sold them on its account. So far as respects the claim to recover the forty per cent. unpaid on the twenty-five shares of stock, we understand it is placed, by the learned counsel for the plaintiff, mainly on the proposition that the capital stock of a corporation is a trust fund for the security of creditors, which cannot be given away or distributed among stockholders so long as debts of the corporation remain unpaid, and that the transaction in question was a violation of this principle. The general principle asserted is, doubtless, well founded, but if it had an appropriate application in the present case, the plaintiff would encounter some difficulty under the authorities in this State, in maintaining a separate action as an individual creditor of the corporation, to reach assets which constitute a trust fund, not for the protection of one creditor only, but equally for all the creditors of the corporation. *Griffith v. Mangam*, 73 N. Y. 611, and cases cited. But passing this, we are of opinion that the forty per cent. credited on the twenty-five shares of stock issued to the defendant Eno cannot be considered as, and does not constitute, a trust fund applicable to the payment of creditors. The capital of a corporation consists of its funds, securities, credits and property of whatever kind which it possesses. The word "capital" applied to corporations is often used interchangeably with the words "capital stock," and both are frequently used to express the same thing—the

property and assets of the corporation. Strictly, the capital stock of a corporation is the money contributed by the corporators to the capital, and is usually represented by shares issued to subscribers to the stock on the initiation of the corporate enterprise. See *Burrall v. Bushwick R. R. C. Co.*, 75 N. Y. 211, 212, and cases cited. It may be admitted that the liability of subscribers on unpaid stock subscriptions constitutes an asset of the corporation, which cannot be surrendered or given up by the corporation without consideration to the prejudice of creditors. It is not claimed that there is any express prohibition in the charter of the bridge company against issuing shares purporting to be fully paid without actual payment. The charter authorizes books of subscription to the stock to be opened. The most that could be claimed from this provision is that by implication it prohibits the issue of stock except to actual subscribers who should undertake to pay the nominal amount of the shares when required. There is no pretense that the defendant Eno ever subscribed for the twenty-five shares of bonus stock (so called), or entered into any engagement to pay the forty per cent. credited thereon. This was distinctly contrary to the intention of all parties. The plaintiff seeks to charge him as though he had subscribed for the stock and entered into a contract obligation with the company to pay the forty per cent. We can see no ground upon which he can be made to respond to the creditors of the company as upon an unpaid subscription. Assuming that the transaction as to the company was *ultra vires*, or that it could not give away its shares, the transaction in that view was simply a nullity, and Eno got nothing as against any one entitled to question the transaction. But it did not convert him into a debtor of the company for the forty per cent. He entered into no contract to pay it. He has received nothing on account of the twenty-five shares, and it is not claimed that the charter in terms imposes the liability claimed. The unissued shares of a corporation are not assets. When issued they represent a proportionate interest of the shareholder in the corporate property—an interest, however, subordinate to the claims of creditors. There are unquestioned public evils growing out of the creation and multiplication of shares of stock in corporations not based upon corporate property. The remedy is with the legislature. But the liability of a shareholder to pay for stock does not arise out of his relation, but depends upon his contract, express or implied, or upon some statute, and in the absence of either of these grounds of liability, we do not perceive how a person to whom shares have been issued as a gratuity has, by accepting them, committed any wrong upon creditors, or made himself liable to pay the nominal face of the shares as upon a subscription or contract. *Seymour v. Sturgess*, 26 N. Y. 134; *In re Western Canada Oil Co.*, L. R. 1 Ch. Div. 115; *Waterhouse v. Jamieson*, 2 L. R. H. L. (Sc.) 29. The question as to the right of the plaintiff to compel the defendant to account for the sum realized by him on the sale of the bonds, is

affected by the fatal difficulty that the defendant has received nothing from the corporation except its promise to pay, which has never been performed. The plaintiff has withdrawn nothing from the funds of the company on account of the bonds (unless it may be a sum represented by a single interest coupon), and creditors have not been prejudiced by the transaction. It is alleged, and it was offered to be proved, that the property of the company had been sold on the foreclosure of the first mortgage. It is unnecessary to consider what the rights or liabilities of the defendant would be in respect to the bonds as between himself and other creditors of the corporation on a distribution of assets, or if it had appeared that the corporation had paid the bonds issued to the defendant. The situation in either of these aspects is not presented. This is not a case of following assets of a corporation wrongfully transferred. The defendant has received none of the funds or assets of the company available to creditors. The loss on the bonds falls on those who have purchased them relying on the credit of the corporation. The situation of the general creditors has not, so far as appears, been affected by the fact that the company received nothing for the bonds. The statute of Missouri, the State from which the bridge company in part derives its existence, authorizes a creditor of a corporation, who shall have obtained judgment against it, upon which an execution has been returned nulla bona, to issue execution thereon against any stockholder to an extent equal in amount to the amount of stock held by him "together with any amount unpaid thereon." The courts of Missouri on an application under this statute for leave to issue execution against a person who was a director and stockholder in the bridge company, who had received bonus stock and bonds, granted the application and came to the conclusion that the forty per cent. credited on the stock could be regarded as the amount unpaid thereon within the statute, and that the amount received on the bonds was also recoverable. *Skrainka v. Allen*, 7 Mo. Rep. 434, 435; s. c., 76 id. 384. The statutory remedy is, of course, not available in this State. *Lowry v. Inman*, 46 N. Y. 119, 120. The court seems to have given much weight to the fiduciary and trust relation existing between a director of a corporation and its creditors. That relation did not exist between the defendant Eno and the creditors of the company. He was a stockholder simply, and no trust relation exists between a stockholder in a corporation and its creditors. The decision in Missouri may stand on its special circumstances, but it is not controlling in the case before us.

We are of opinion that the judgment appealed from is erroneous and that it should, therefore, be reversed and new trial ordered.

All concur.

*Judgment reversed.**

*In *Currie's Case* (1862) 3 DeG. J. & S. 367, held that in the case of the allotment of paid up shares in part payment of the purchase price of property, the transaction could not be affirmed and repudiated in part, and that,

HANDLEY v. STUTZ.

1891. 139 U. S. 417, 35 L. ed. 227, 11 Sup. Ct. 530.*

THIS was a bill in equity filed by judgment creditors of the Clifton Coal Company on behalf of themselves and such other creditors of the company as should come in and contribute to the expenses of the suit, against the Clifton Coal Company and certain of its stockholders, to compel the assessment upon certain shares of stock held by the individual defendants, and payment of the same as a trust fund for the satisfaction of the debts of the company. * * *

It further appeared from the testimony that the company was organized soon after its articles of incorporation were filed; that its chief office was at Mannington, Kentucky; and that it began business at once and made large outlays and expenditures for machinery, buildings, materials and labor. In the early part of the year 1886, the company was led to believe that its coal would coke, and therefore its products could be profitably extended from grate and steam purposes to iron-making coke. To embark in the manufacture of coke, however, money was needed, and a meeting of the stockholders was held March 31, 1886, at which a resolution was passed, reciting that \$50,000 was needed with which to erect coke ovens, buildings, improvements, etc., to further develop the property; and it was unanimously resolved to issue \$50,000 of bonds of the company, in sums of \$1,000 each, due thirty years from April 1, with 6 per cent. interest, and secured by trust mortgage upon the property of the company, and the president was authorized to dispose of such bonds as in his discretion seemed best. The mortgage was executed to the designated trustee and recorded. It was found, however, that the bonds could not be sold, and to meet the demands upon the company for money, it borrowed a large amount upon its notes, indorsed by its directors and stockholders and to secure the lenders and indorsers, the \$50,000 of bonds were deposited in two banks in Nashville, Tennessee, as additional collateral security for the loans. Finding that no one would purchase the bonds, and being advised that in order to effect their sale it would be better to add an equal amount of stock to the bonds, and propose to the purchasers of such bonds to give as a gratuity \$1,000 of stock with each \$1,000 bond, a meeting of the stockholders of the company was held at Nashville, May 31, 1886, at which all the stockholders were present in person or by proxy, although without any call or previous notice and "it was unanimously resolved that the capital stock of the company be increased to \$200,000, as authorized by the charter."

consequently, the directors, if treated as shareholders at all, must be treated as paid up shareholders and not liable to creditors. See also, *Continental Adjustment Co. v. Cook* (1907) 152 Fed. 652. Cf. *De Ruigne's Case* (1877) L. R. 5 Ch. Div. 306.—Eds.

* Portion of statement of facts omitted. Only the portion of opinion relating to "watered stock" given.—Eds.

This resolution was not then entered upon the records of the corporation, but was formulated in the shape of a pencil memorandum, and adopted unanimously, although no vote appeared to have been taken, and no formal record was made of the meeting until the summer of 1888. No notice of such change in the amount of its capital stock was recorded or published, as required by the laws of Kentucky. The subscribers to the bonds subsequently executed the agreement set forth in the bill, and bonds to the amount of \$45,000 were delivered to the subscribers with equal amounts of certificates of "paid-up" stock, the receipts reciting that it "was issued with bonds for same amount, as per agreement." The certificates on their face recited that the shares of stock were fully paid up "and were non-assessable," or language to that effect. Five thousand dollars of the bonds were left in one of the national banks at Nashville as collateral security for a loan to the company, no one having subscribed for them. The remaining \$30,000 shares of increased stock, which were not needed to secure the subscribers to the bonds, appeared to have been distributed *pro rata* among the old stockholders. In the latter part of 1887, and in the early part of the following year, plaintiff obtained judgments against the company, which were unsatisfied, and in September, 1887, by an order of the Circuit Court of Hopkins County, Kentucky, the entire property of the company was placed in the hands of a receiver, and its operation stopped.

* * * * *

MR. JUSTICE BROWN delivered the opinion of the court: * * *

So far as the question of liability to the proposed assessments is concerned, these defendants, with respect to their relations to this corporation, are divisible into two distinct classes: *First*, those of the original stockholders who received the \$30,000 increased stock as a gift; *second*, those who subscribed to the \$50,000 bonds, and received an equal amount of stock as a bonus or inducement to make the subscription.

With regard to the first class, namely, the original stockholders, who voted for this increase of shares, and then distributed among themselves 300 of those shares, without the shadow of right or consideration, it is difficult to see why they could not be called upon to respond for their value. The only claim made upon their behalf is that they never agreed to contribute or pay for the same; that the stock was expressly declared to be "fully paid" and "free from all claims or demands upon the part of the company;" that there was no evidence that the creditors of the company knew of, or relied upon, this increase, in their dealings with the company; and that they had a right to return and surrender the same, which they offered to do. There is no reason to suppose that these stockholders did not act in good faith, and in the belief that they were entitled to this stock. The fact that they did not subscribe for it or agree to take it until the receipt of the certificates is immaterial, as the acceptance of the certificates is sufficient evidence of an agreement to pay their

par value. *Sanger v. Upton*, 91 U. S. 56, 64; *Chubb v. Upton*, 95 U. S. 665; *Brigham v. Mead*, 10 Allen 245.

Ever since the case of *Sawyer v. Hoag*, 17 Wall. (U. S.) 610, it has been the settled doctrine of this court that the capital stock of an insolvent corporation is a trust fund for the payment of its debts; that the law implies a promise by the original subscribers of stock who did not pay for it in money or other property to pay for same when called upon by creditors; and that a contract between themselves and the corporation, that the stock shall be treated as fully paid and non-assessable, or otherwise limiting their liability therefor, is void as against creditors. The decisions of this court upon this subject have been frequent and uniform, and no relaxation of the general principle has been admitted. *Upton v. Tribilcock*, 91 U. S. 45; *Sanger v. Upton*, 91 U. S. 56; *Webster v. Upton*, 91 U. S. 65; *Chubb v. Upton*, 95 U. S. 665; *Pullman v. Upton*, 96 U. S. 328; *Morgan County v. Allen*, 103 U. S. 498; *Hawkins v. Glenn*, 131 U. S. 319; *Graham v. La Crosse & M. R. Co.*, 102 U. S. 148, 161; *Richardson v. Green*, 133 U. S. 30.

It is simply in affirmation of this general principle that section 14, chapter 56, of the General Statutes of Kentucky declares that nothing in the Act conferring corporate franchises, or permitting the organization of corporations, "shall exempt the stockholders of any corporation from individual liability to the amount of the unpaid installments on stock owned by them." If the corporation has no right, as against creditors, to sell or dispose of this stock with an agreement that no further assessment shall be made upon it, much less has it the right to give it away, or distribute it among shareholders, without receiving a fair equivalent therefor, and thereby induce the public to deal with it upon the credit of such shares, as representing the assets of the corporation. *Upton Mutual L. Ins. Co. v. Free Stone Mfg. Co.*, 97 Ill. 537. The stock of a corporation is supposed to stand in the place of actual property of substantial value, and as being a convenient method of representing the interest of each stockholder in such property, and to the extent to which it fails to represent such value, it is either a deception and fraud upon the public, or an evidence that the original value of the corporate property has become depreciated. The market value of such shares rises with an increase in the value of the corporate assets, and falls in case of loss or misfortune, whereby the value of such assets is impaired. And the increase of value of such stock is taken to represent either an appreciation in value of the company's property beyond the par value of the original shares, or so much money paid to the corporation as is represented by such shares. If it be once admitted that a corporation may issue stock without receiving a consideration therefor, and where it does not represent actual or substituted value in corporate assets, there is apparently no limit to the extent to which the original stock may be "watered," except the caprice of the stockholders. While an agreement that the sub-

scribers or holders of stock shall never be called upon to pay for the same may be good as against the corporation itself, it has been uniformly held by this court not to be binding upon its creditors.

Somewhat different considerations apply to those who subscribed for the bonds of the company, with the understanding that they were to receive an amount of stock equal to the bonds as an additional inducement to their subscription. The facts connected with this transaction are substantially as follows: Some three years after the company was organized it became apparent that the enterprise, as originally contemplated, namely the mining and selling of coal for steam and domestic purposes, was not likely to be a success, owing to the inferior character of the product; and the only hope of the company lay in the manufacture of the coal into an iron-making coke, that is, a coke containing a percentage of sulphur low enough to admit of the manufacture of merchantable pig-iron. To embark in this, however, money was needed, and as the stock of the company was not worth more than fifty cents on the dollar, it was evident this could not be effected simply by the issue of new stock. It was proposed at the meeting in March that money should be raised by the issue of \$50,000 of bonds, with which to add the requisite structures to the plant. But it was soon evident that the bonds could not be negotiated without the stock, and acting upon the suggestion of a Nashville banker, it was resolved at the meeting in May that the stock should be increased 800 shares, 500 of which should be turned over to the subscribers to the bonds, as a bonus or an additional consideration. The evidence is uncontradicted that the bonds could not have been negotiated without the stock; that they were both sold as whole; that the transaction was in good faith, and, considering the risk that was taken by the subscribers, the price paid for the stock and bonds was fair and reasonable. The directors appear to have done all in their power to obtain the best possible terms, and there is no imputation of unfair dealing on the part of anyone connected with the transaction. At that time the mines and property of the company were in good condition, and the prospects of success were fair.

The case then resolves itself into the question whether an active corporation, or, as it is called in some cases, a "going concern," finding its original capital impaired by loss or misfortune, may not, for the purpose of recuperating itself and providing new conditions for the successful prosecution of its business, issue new stock, put it upon the market and sell it for the best price that can be obtained. The question has never been directly raised before in this court, and we are not, consequently, embarrassed by any previous decisions on the point. In the Upton Cases arising out of the failure of the Great Western Insurance Company, in *Hatch v. Dana*, 101 U. S. 205, and in *Hawkins v. Glenn*, 131 U. S. 319, the defendants were either original subscribers to the increased stock, at a price far below its par value, or transferees of such subscribers; and the stock

was issued, not as in this case, to purchase property or to raise money, to add to the plant and facilitate the operations of the company, but simply to increase its original stock in order to carry on a larger business, and the stock thus issued was treated as if it formed a part of the original capital. In *Morgan County v. Allen*, 103 U. S. 498, the same principle was applied to a subscription by a county to the capital stock of a railroad company, for which it had issued its bonds, although such bonds had been surrendered to the county with the consent of certain of its creditors.

To say that a corporation may not, under the circumstances above indicated, put its stock upon the market and sell it to the highest bidder, is practically to declare that a corporation can never increase its capital by a sale of shares, if the original stock has fallen below par. The wholesome doctrine, so many times enforced by this court, that the capital stock of an insolvent corporation is a trust fund for the payment of its debts, rests upon the idea that the creditors have a right to rely upon the fact that the subscribers to such stock have put into the treasury of the corporation in some form, the amount represented by it; but it does not follow that every creditor has a right to trace each share of stock issued by such corporation, and inquire whether its holder, or the person of whom he purchased has paid its par value for it. It frequently happens that corporations, as well as individuals, find it necessary to increase their capital in order to raise money to prosecute their business successfully, and one of the most frequent methods resorted to is that of issuing new shares of stock and putting them upon the market for the best price that can be obtained; and so long as the transaction is bona fide, and not a mere cover for 'watering' the stock, and the consideration obtained represents the actual value of such stock, the courts have shown no disposition to disturb it. Of course no one would take stock so issued at a greater price than the original stock could be purchased for, and hence the ability to negotiate the stock and to raise the money must depend upon the fact whether the purchaser shall or shall not be called upon to respond for its par value. While, as before observed, the precise question has never been raised in this court, there are numerous decisions to the effect that the general rule that holders of stock, in favor of creditors must respond for its par value, is subject to exceptions where the transaction is not a mere cover for an alleged increase. * * *

A case nearer in point is that of *Clark v. Bever*, 139 U. S. 96, decided at the present term of this court. In this case, a railroad company, of which defendant's intestate was president and stockholder, had a settlement with a construction company, of which defendant's intestate was also a member, for work done in building the road. The railroad company, being unable to pay the claim of the construction company, delivered to it thirty-five hundred shares of its stock at 20 cents on the dollar, and the same were accepted in full satisfaction of the debt. The stock was not worth anything in the

market, and was issued directly to the defendant's intestate. No other payment than the 20 per cent. was ever made on account of this stock. A judgment creditor of the railroad company filed a bill to compel the payment by the defendant of his claim upon the theory that he was liable for the actual par value of such stock, whatever may have been its market value at the time it was received. It was held he could not recover. "Of course under this view," said Mr. Justice Harlan, in delivering the opinion of the court, "everyone having claim against the railway company,—even laborers and employes,—who could get nothing except stock in payment of their demands, became bound, by accepting stock at its market value in payment, to account to unsatisfied judgment creditors for its full face value, although, at the time it was sought to make them liable, the corporation had ceased to exist, and its stock had ceased to exist, and its stock had remained, as it was when taken, absolutely worthless. * * * To say that a public corporation, charged with public duties, may not relieve itself from embarrassment by paying its debt in stock at its real value,—there being no statute forbidding such a transaction,—without subjecting the creditor, surrendering its debt, to the liability attaching to stockholders who have agreed, expressly or impliedly to pay the face value of stock subscribed by them, is, in effect, to compel them either to suspend operations the moment they become unable to pay their current debts or to borrow money secured by mortgage upon the corporate property."

So in *Fogg v. Blair*, 139 U. S. 118, also decided at the present term, it was held to be competent for a railroad, exercising good faith, to use its bonds or stock in payment for the construction of its road, although it could not, as against creditors or stockholders, issue its stock as fully paid without getting some fair or reasonable equivalent for it. It was there said: "What was such an equivalent depends primarily upon the actual value of the stock at the time it was contracted to be issued, and upon the compensation which, under all the circumstances, the contractors were equitably entitled to receive for the particular work undertaken or done by them." It appeared in that case that full and adequate compensation for the work done had been paid by the company in its mortgage bonds, and, as the bill contained no allegation whatever as to the real or market value of such stock, it was held that the contractors receiving this stock were not liable to creditors for its par value. It was added: "If, when disposed of by the railroad company, it was without value, no wrong was done to creditors by the contract made with Blair and Taylor. If the plaintiff expected to recover in this suit on the ground that the stock was of substantial value, it was incumbent upon him to distinctly allege facts that would enable the court—assuming such facts to be true—to say that the contract between him and the railroad company and the contractors was one which, in the interest of creditors, ought to be closely scrutinized." It would seem to follow from this that if the stock had been of some

value, that value, however much less than par, would have been the limit of the holders' liability.

In *Morrow v. Nashville I. S. Co.*, 87 Tenn. 262, the Supreme Court of Tennessee held that a contract with a subscriber to stock of a corporation, that for every share subscribed he should receive bonds to an equal amount, secured by mortgage on the company's plant, is void as against creditors, and also between the subscriber and the corporation. But the court drew distinction between such a case and sales of or subscription to the stock of an organized and going corporation. It said: "The necessities of the business of an organized company might demand an increase of capital stock, and if such stock is lawfully issued, it may very well be offered upon special terms. In such case, if the market price was less than par, it is clear that a purchaser or subscriber for such stock at its market value would, in the absence of fraud, be liable only for his contract price. So a case might arise where the stock of a going concern was much depreciated, and where its bonds were likewise below par, and there was lawful authority to issue additional stock and bonds. Now, in such case, the real market value of an equal amount of stock and bonds might not exceed, or even equal the par value of either. In such cases, the question of fraud aside, the purchaser would only be held for his contract price." This case from Tennessee puts as an illustration the exact case with which we are now dealing.

The liability of a subscriber for the par value of increased stock taken by him may depend somewhat on the circumstances under which, and the purpose for which, such increase was made. If it be merely for the purpose of adding to the original capital stock of the corporation, and enabling it to do a larger and more profitable business, such subscriber would stand practically upon the same basis as a subscriber to the original capital. But we think that an active corporation may, for the purpose of paying its debts, and obtaining money for the successful prosecution of its business, issue its stock and dispose of it for the best price that can be obtained. *Stein v. Howard*, 65 Cal. 616. As the company in this case found it impossible to negotiate its bonds at par without the stock, and as the stock was issued for the purpose of enhancing the value of the bonds, and was taken by the subscribers to the bonds at a price fairly representing the value of both stocks and bonds, we think the transaction should be sustained, and that the defendants cannot be called upon to respond for the par value of such stock, as if they had subscribed to the original stock of the company. Our conclusion upon this branch of the case disposes of it as to those who were held liable by virtue of their subscription to the bonds.

We have no doubt the learned circuit judge held correctly that it was only subsequent creditors who were entitled to enforce their claims against these stockholders, since it is only they who could, by any legal presumption, have trusted the company upon the faith

of the increased stock. *First Nat. Bank of Deadwood v. Gustin Minerva Con. Min. Co.*, 42 Minn. 327; 2 Morawetz on Corporations, §§ 832, 833; *Coit v. North Carolina Gold Amalgamating Co.*, 14 Fed. Rep. 12. We also agree with him that creditors, who became such after the increase was voted in May, 1886, are entitled to look to those who subsequently received the stock, notwithstanding they did not receive it until after the debts had been contracted. The circuit judge found in this connection that the "complainants had no knowledge or notice of the subscription paper of December 30, 1880, under which \$45,000 of the new stock was distributed to those who subscribed for bonds, nor of the distribution among the old stockholders of \$30,000 of said increased stock; nor does it affirmatively appear that they or either of them dealt with and trusted the company upon the faith of that increased stock; but the fact that the capital stock had been increased to \$200,000 was made public and was generally known." The real question in this connection is, When may it be presumed creditors trusted the corporation upon the faith of the increased stock? Obviously, when such increase was ordered. That is a fact to which publicity would naturally be given; the creditors could not be expected to know when and by whom such stock would be taken. It is true they assume the risk of the stock not being taken at all, but the moment shares are taken, they are supposed to represent so much money put into the treasury as they are worth, which becomes available for the payment, not only of future, but of existing, creditors. It is manifest that any attempt to gauge the liability of stockholders by the exact time they took their stock with reference to the dates when the several claims of the creditors accrued, and by the further fact whether the creditors actually knew of and relied upon such stock, would in case like this, where the creditors and stockholders are both numerous, lead into inextricable confusion. Even the flexibility of a court of equity would be inadequate to adjust the rights of the parties. * * *

It results that the decree of the court below must be reversed and the cause remanded for further proceedings in conformity with this opinion.

MR. CHIEF JUSTICE FULLER, with whom concurring MR. JUSTICE LAMAR, dissenting:

I dissent from the conclusion of the court in respect of the stock received by the subscribers to the bonds. That stock was not paid for in money or money's worth, or issued in payment of debts due from the company, or purchased at sale upon the market. It was a mere bonus, thrown in with the bonds as furnishing the inducement to the bond subscription, of larger control over the corporation, and of possible gain without expenditure. Becoming secured creditors through the bonds, the subscribers increased their power through the stock. In my view, there was no actual payment for the stock, and to treat it as paid up is to sanction an arrangement to relieve those who could reap the benefit derived from the possession

of the stock, in the event of the success, from liability for the consequences, in the event of the failure, of the enterprise.

When the capital stock of a corporation has become impaired, or the business in which it has engaged has proven so unremunerative as to call for a change, creditors at large may well demand that experiments at rehabilitation should not be conducted at their risk.

My brother LAMAR concurs with me in this dissent.⁷

HOSPES v. NORTHWESTERN MFG. & CAR CO.

1892. 48 Minn. 174, 50 N. W. 1117, 15 L. R. A. 470, 31 Am. St. 637.⁸

APPEAL from order overruling demurrer to supplemental complaint.

MITCHELL, J. * * * The principal question in the case is whether the complaint states facts showing that the thrasher company, as creditor, is entitled to the relief prayed for; or, in other words, states a cause of action. Briefly stated, the allegations of the complaint are that on May 10, 1882, Seymour, Sabin & Co. owned property of the value of several million dollars, and a business then supposed to be profitable. That, in order to continue and enlarge this business, the parties interested in Seymour, Sabin & Co., with others, organized the car company, to which was sold the greater part of the assets of Seymour, Sabin & Co. at a valuation of \$2,267,000, in payment of which there were issued to Seymour, Sabin & Co. shares of the preferred stock of the car company of the par value of \$2,267,000, it being then and there agreed by both parties that this stock was in full payment of the property thus purchased. It is further alleged that the stockholders of Seymour, Sabin & Co., and the other persons who had agreed to become stockholders in the car company, were then desirous of issuing to themselves, and obtaining for their own benefit, a large amount of common stock of the car company, "without paying therefor, and without incurring any liability thereon or to pay therefor;" and for that purpose, and "in order to evade and set at naught the laws of this state," they caused Seymour, Sabin & Co. to subscribe for and agree to take common stock of the car company of the par value of \$1,500,000. That Seymour, Sabin & Co. thereupon subscribed for that

⁷ See *Bent, Receiver, v. Underdown* (1901) 156 Ind. 516, 60 N. E. 307; *Drummer v. Smedley* (1896) 110 Mich. 466, 68 N. W. 260; *Kraft v. Griffon Co.* (1903) 82 App. Div. (N. Y.) 29, 81 N. Y. S. 438; *Rickerson Roller-Mill Co. v. Farrell Foundry & Machine Co.* (1896) 75 Fed. 554, 23 C. C. A. 302; *Scovill v. Thayer* (1881) 105 U. S. 143, at p. 154, 26 L. ed. 968, at 973. See also article by G. W. Wickersham, 22 Harv. Law. Rev. 319, 330-3.—Eds.

⁸ The opinion sufficiently states the facts. A slight portion of opinion omitted.—Eds.

amount of the common stock, but never paid therefor any consideration whatever, either in money or property. That thereafter these persons caused this stock to be issued to D. M. Sabin as trustee, to be by him distributed among them. That it was so distributed without receipt by him or the car company, from any one, of any consideration whatever, but was given by the car company and received by these parties entirely "gratuitously." The car company was at this time free from debt, but afterwards became indebted to various persons for about \$3,000,000. The thrasher company, incorporated after the insolvency and receivership of the car company, for the purpose of securing possession of its assets, property and business, and therewith engaging in and continuing the same kind of manufacturing, prior to October 27, 1887, purchased and became the owner of unsecured claims against the car company, "bona fide, and for a valuable consideration," to the aggregate amount of \$1,703,000. As creditor, standing on the purchase of these debts, which were contracted after the issue of this "bonus" stock, the thrasher company files this complaint to recover the par value of the stock as never having been paid for. The complaint does not allege what the consideration of these debts was, nor to whom originally owing, nor what the intervener paid for them, nor whether any of the original creditors trusted the car company on the faith of the bonus stock having been paid for. Neither does it allege that either the thrasher company or its assignors were ignorant of the bonus issue of stock, nor that they or any of them were deceived or damaged in fact by such issue, nor that the bonus stock was of any value. Neither is there any traversable allegation of any actual fraud or intent to deceive or injure creditors. A desire to get something without paying for it, and actually getting it, is not fraudulent or unlawful if the donor consents, and no one else is injured by it; and the general allegation that it was done "in order to evade and set at naught the laws of the state" of itself amounts to nothing but a mere conclusion of law. As a creditor's bill, in the ordinary sense, the complaint is manifestly insufficient. The thrasher company, however, plants itself upon the so-called "trust-fund" doctrine, that the capital stock of a corporation is a trust fund for the payment of its debts; its contention being that such a "bonus" issue of stock creates, in case of the subsequent insolvency of the corporation, a liability on the part of the stockholder in favor of creditors to pay for it, notwithstanding his contract with the corporation to the contrary.

This "trust-fund" doctrine, commonly called the "American doctrine," has given rise to much confusion of ideas as to its real meaning, and much conflict of decision in its application. To such an extent has this been the case that many have questioned the accuracy of the phrase, as well as doubted the necessity or expediency of inventing any such doctrine. While a convenient phrase to express a certain general idea, it is not sufficiently precise or accurate to constitute a safe foundation upon which to build a system of legal rules.

The doctrine was invented by Justice Story in *Wood v. Dummer*, 3 Mason 308, which called for no such invention, the fact in that case being that a bank divided up two-thirds of its capital among its stockholders without providing funds sufficient to pay its outstanding billholders. Upon old and familiar principles this was a fraud on creditors. Evidently all that the eminent jurist meant by the doctrine was that corporate property must be first appropriated to the payment of the debts of the company before there can be any distribution of it among stockholders,—a proposition that is sound upon the plainest principles of common honesty. In *Fogg v. Blair*, 133 U. S. 534, 541 (10 Sup. Ct. Rep. 338,) it is said that this is all the doctrine means. The expression used in *Wood v. Dummer* has, however, been taken up as a new discovery, which furnished a solution of every question on the subject. The phrase that “the capital of a corporation constitutes a trust fund for the benefit of creditors” is misleading. Corporate property is not held in trust, in any proper sense of the term. A trust implies two estates or interests,—one equitable and one legal; one person, as trustee, holding the legal title, while another, as the cestui que trust, has the beneficial interest. Absolute control and power of disposition are inconsistent with the idea of a trust. The capital of a corporation is its property. It has the whole beneficial interest in it, as well as the legal title. It may use the income and profits of it, and sell and dispose of it, the same as a natural person. It is a trustee for its creditors in the same sense and to the same extent as a natural person, but no further. This is well illustrated and clearly announced in the case of *Graham v. La Crosse & M. R. Co.*, 102 U. S. 148. That was a creditors’ suit to reach a piece of real estate on the ground that it had been conveyed by the corporation fraudulently for a wholly inadequate consideration. The trust-fund doctrine was invoked by a subsequent creditor, and it was claimed that, as the trust had been violated, the deed should be set aside. If the premise was correct that the corporation held it in trust for creditors, the conclusion was inevitable; but the court denied the premise, saying that a corporation is in law as distinct a being as an individual is, and is entitled to hold property (if not contrary to its charter) as absolutely as an individual can hold it. Its estate is the same, its interest is the same, its possession is the same; and that there is no reason why the disposal by a corporation of any of its property should be questioned by subsequent creditors any more than a like disposal by an individual; that the same principles of law apply to each. That the phrase that “the capital of a corporation is a trust fund for the payment of its creditors” is misleading, if not inaccurate, is illustrated by the character of the actions that are frequently mistakenly instituted on the strength of it. For example, in the case of *Wabash, etc., R. Co. v. Ham*, 114 U. S. 587 (5 Sup. Ct. Rep. 1081,) two roads had been consolidated, the new company acquiring the property of the old ones. A creditor of one of the old companies,

on the strength of the "trust-fund" doctrine, claimed a lien on its property in the hands of the new corporation. If this property was impressed with a trust in favor of creditors in the hands of the old company, it would logically follow that it would continue so in the hands of the new one. But the court denied the relief, and, in giving its construction of the "trust-fund" doctrine, said: "The property of a corporation is doubtless a trust fund for the payment of its debts in the sense that when the corporation is lawfully dissolved, and all its business wound up, or when it is insolvent, all its creditors are entitled in equity to have their debts paid out of the corporate property before any distribution thereof among the stockholders. It is also true, in the case of a corporation, as in that of a natural person, that any conveyance of the property of the debtor without authority of law and in fraud of existing creditors is void." This is probably what is meant when it is said in some cases, as in *Clark v. Bever*, 139 U. S. 96, 110 (11 Sup. Ct. Rep. 468,) that the capital of a corporation is a trust fund *sub modo*. If so, no one will dispute it. But it means very little, for the same thing could be truthfully said of the property of an individual or a partnership. And obviously it would make no difference whether the disposition of the corporate property is to a stranger or to a stockholder, except that, of course, the latter could not be an innocent purchaser.

There is also much confusion in regard to what the "trust-fund" doctrine applies. Some cases seem to hold that unpaid subscribed capital is a trust fund, while other assets are not,—that is, so long as the subscription is unpaid, it is held in trust by the corporation, but, when once paid in, it ceases to be a trust fund; while other cases hold that, paid or unpaid, it is all a trust fund. The first seems to be the rule laid down in *Sawyer v. Hoag*, 17 Wall. 610, in which the "trust-fund" doctrine was first squarely announced by that court with all the vigor and force characteristic of the great jurist who wrote the opinion. In that case a stockholder in an insurance company had given his note, as the court found the fact to be, for 85 per cent. of his subscription to the stock of the company. After the company had become bankrupt, and the stockholder knew the fact, he brought up a claim against the company for one-third its face, and in a suit by the assignee in bankruptcy on his note set up this claim as an offset. That this would have been a fraud on the bankrupt act, and at least a moral fraud on policy holders, is quite apparent without invoking the "trust-fund" doctrine; and, if the note for unpaid stock was a trust fund, there could have been no offset, whether the company was solvent or insolvent. In the opinion it is said that, if the subscription had been paid by the note or otherwise, the note ceased thereby to be a trust fund to which creditors can look, and becomes ordinary assets, with which directors may deal as they choose. But in *Upton v. Tribilcock*, 91 U. S. 45, it is stated: "The capital paid in and promised to be paid in is a fund which the trustees cannot squander or give away."

While in *Sanger v. Upton*, Id. 56, it is said: "When debts are incurred a contract arises with the creditors that it (the capital) shall not be withdrawn or applied otherwise than upon their demands until such demands are satisfied." And in the same connection it is distinctly stated that there is no difference between assets paid in and subscriptions; that "unpaid stock is as much a part of this pledge and as much a part of the assets of the company as the cash which has been paid in upon it. Creditors have the same right to look to it as to anything else, and the same right to insist upon its payment as upon the payment of any other debt due to the company. *As regards creditors, there is no distinction between such a demand and any other asset which may form a part of the property and effects of the corporation.*" This language is quoted and approved in *County of Morgan v. Allen*, 103 U. S. 498, 508. It would seem clear that this is the correct statement of the law. The capital (not the mere share certificates) means all the assets, however invested. If a subscriber gives his note for his stock, that note is no more and no less a trust fund than the money would have been if he had paid cash down. Capital cannot change from a trust to not a trust by a mere change of form. It is either all a trust or all not a trust, and the "trust-fund" rule, whatever that be, must apply to all alike, and in the same way. If the assets of a corporation are given back to stockholders, the result is the same as if the shares had been issued wholly or partly as a bonus. The latter is merely a short cut to the same result. So with dividends paid out of the capital, voluntary conveyances, stock paid in overvalued property; all are forms of one and the same thing, all reaching the same result (a disposition of corporate assets,) which may or may not be a fraud on creditors, depending on circumstances. This much being once settled, the solution of the question when a subsequent creditor can insist on payment of stock issued as paid up, but not in fact paid for, or not paid for at par, becomes, as we shall presently see, comparatively simple.

Another proposition which we think must be sound is that creditors cannot recover on the ground of contract when the corporation could not. Their right to recover in such cases must rest on the ground that the acts of the stockholders with reference to the corporate capital constitutes a fraud on their rights. We have here a case where the contract between the corporation and the takers of the shares was specific that the shares should not be paid for. Therefore, unlike many of the cases cited, there is no ground for implying a promise to pay for them. The parties have explicitly agreed that there shall be no such implication, by agreeing that the stock shall not be paid for. In such a case the creditors undoubtedly may have rights superior to the corporation, but these rights cannot rest on the implication that the shareholder agreed to do something directly contrary to his real agreement, but must be based on tort or fraud, actual or presumed. In England, since the act of 1867, there

is an implied contract created by statute that "every share in any company shall be deemed and be taken to have been issued and to be held subject to the payment of the whole amount thereof in cash." This statutory contract makes every contrary contract void. Such a statute would be entirely just to all, for every one would be advised of its provisions, and could conduct himself accordingly. And in view of the fact that "watered" and "bonus" stock is one of the greatest abuses connected with the management of modern corporations, such a law might, on grounds of public policy, be very desirable. But this is a matter for the legislature, and not for the courts. We have no such statute; and, even if the law of 1873, under which the car company was organized, impliedly forbids the issue of stock not paid for, the result might be that such issue would be void as *ultra vires*, and might be cancelled, but such a prohibition would not of itself be sufficient to create an implied contract, contrary to the actual one, that the holder should pay for his stock.

It is well settled that an equity in favor of a creditor does not arise absolutely and in every case to have the holder of "bonus" stock pay for it contrary to his actual contract with the corporation. Thus no such equity exists in favor of one whose debt was contracted prior to the issue, since he could not have trusted the company upon the faith of such stock. *First Nat. Bank v. Gustin, etc., Mining Co.*, 42 Minn. 327, (44 N. W. Rep. 198); *Coit v. Gold Amalgamating Co.*, 119 U. S. 343, (7 Sup. Ct. Rep. 231); *Handley v. Stutz*, 139 U. S. 417, 435, (11 Sup. Ct. Rep. 530). It does not exist in favor of a subsequent creditor who has dealt with the corporation with full knowledge of the arrangement by which the "bonus" stock was issued, for a man cannot be defrauded by that which he knows when he acts. *First Nat. Bank v. Gustin, etc., Mining Co.*, supra. It has also been held not to exist where the stock has been issued and turned out at its full market value to pay corporate debts. *Clark v. Bever*, supra. The same has been held to be the case where an active corporation, whose original capital has been impaired, for the purpose of recuperating itself issues new stock, and sells it on the market for the best price obtainable, but for less than par (*Handley v. Stutz*, supra); although it is difficult to perceive, in the absence of a statute authorizing such a thing (of which every one dealing with corporations is bound to take notice), any difference between the original stock of a new corporation and additional stock issued by a "going concern." It is difficult, if not impossible, to explain or reconcile these cases upon the "trust-fund" doctrine, or, in the light of them, to predicate the liability of the stockholder upon that doctrine. But by putting it upon the ground of fraud, and applying the old and familiar rules of law on that subject to the peculiar nature of a corporation and the relation which its stockholders bear to it and to the public, we have at once rational and logical ground on which to stand. The capital of a corporation is the basis of its credit. It is a substitute for the individual liability of those

who own its stock. People deal with it and give it credit on the faith of it. They have a right to assume that it has paid-in capital to the amount which it represents itself as having; and if they give it credit on the faith of that representation, and if the representation is false, it is a fraud upon them; and in case the corporation becomes insolvent, the law, upon the plainest principles of common justice, says to the delinquent stockholder, "Make that representation good by paying for your stock." It certainly cannot require the invention of any new doctrine in order to enforce so familiar a rule of equity. It is the misrepresentation of fact in stating the amount of capital to be greater than it really is that is the true basis of the liability of the stockholder in such cases; and it follows that it is only those creditors who have relied, or who can fairly be presumed to have relied, upon the professed amount of capital, in whose favor the law will recognize and enforce an equity against the holders of "bonus" stock. This furnishes a rational and uniform rule, to which familiar principles are easily applied, and which frees the subject from many of the difficulties and apparent inconsistencies into which the "trust-fund" doctrine has involved it; and we think that, even when the trust-fund doctrine has been invoked, the decision in almost every well-considered case is readily referable to such a rule.

It is urged, however, that, if fraud be the basis of the stockholders' liability in such cases, the creditor should affirmatively allege that he believed that the bonus stock had been paid for, and represented so much actual capital, and that he gave credit to the corporation on the faith of it; and it is also argued that, while there may be a presumption to that effect in the case of a subsequent creditor, this is a mere presumption of fact, and that in pleadings no presumptions of fact are indulged in. This position is very plausible, and at first sight would seem to have much force; but we think it is unsound. Certainly any such rule of pleading or proof would work very inequitably in practice. Inasmuch as the capital of a corporation is the basis of its credit, its financial standing and reputation in the community has its source in, and is founded upon, the amount of its professed and supposed capital, and every one who deals with it does so upon the faith of that standing and reputation, although, as a matter of fact, he may have no personal knowledge of the amount of its professed capital, and in a majority of cases knows nothing about the shares of stock held by any particular stockholder, or, if so, what was paid for them. Hence, in a suit by such creditor against the holders of "bonus" stock, he could not truthfully allege, and could not affirmatively prove, that he believed that the defendants' stock had been paid for, and that he gave the corporation credit on the faith of it, although, as a matter of fact, he actually gave the credit on the faith of the financial standing of the corporation, which was based upon its apparent and professed amount of capital. The misrepresentation as to the amount of capital would operate as a

fraud on such a creditor as fully and effectually as if he had personal knowledge of the existence of the defendants' stock, and believed it to have been paid for when he gave the credit. For this reason, among others, we think that all that it is necessary to allege or prove in that regard is that the plaintiff is a subsequent creditor; and that, if the fact was that he dealt with the corporation with knowledge of the arrangement by which the "bonus" stock was issued, this is a matter of defence. *Gogebic Inv. Co. v. Iron Chief Min. Co.*, 78 Wis. 427, (47 N. W. Rep. 726). Counsel cites *Fogg v. Blair*, *supra*, to the proposition that the complaint should have stated that this stock had some value; but that case is not in point, for the plaintiff there was a prior creditor; and, as his debt could not have been contracted on the faith of stock not then issued, he could only maintain his action, if at all, by alleging that the corporation parted with something of value.

In one respect, however, we think the complaint is clearly insufficient. The thrasher company is here asking the interposition of the court to aid in enforcing an equity in favor of creditors against the stockholders by declaring them liable to pay for this stock contrary to their actual contract with the corporation. While the proceeding is not, strictly speaking, an equitable action, yet the relief asked is equitable in its nature. Under such circumstances, it was incumbent upon the thrasher company to show its own equities, and that it was in a position to demand such relief. It was not the original creditor of the car company, but the assignee of the original creditors. By that purchase it, of course, succeeded to whatever strictly legal rights its assignors had; but it is not rights of that kind which it is here seeking to enforce. Under such circumstances, we think it was incumbent upon it to state what it paid for the claims, or at least to show that it paid a substantial, and not a mere nominal, consideration. The only allegation is that it paid "a valuable consideration." This might have been only one dollar. It appears that it bought the claims after the car company had become insolvent, and its affairs were in the hands of a receiver; also that the indebtedness of that company amounted to about \$3,000,000, and that there were not corporate assets enough to pay any considerable part of it. The mere chance of collecting something out of the stockholders does not ordinarily much enhance the selling price of claims against an insolvent corporation. If any person or company had gone to work and bought up for a mere song this large indebtedness of the car company for the purpose of speculating on the liability of the stockholders, no court would grant them the relief here prayed for. It would say to them: "We will not create and enforce an equity for the benefit of any such speculation." Counsel for respondent suggests that the thrasher company is but an organization of the original creditors, who formed it, and pooled their claims, so as to save something out of the wreck of the car company; but nothing of the

kind is alleged. On this ground the demurrer should have been sustained. * * *

Order reversed.

GILFILLAN, C. J., took no part.*

(3) *Rights of Creditors Against Holders of Stock Issued for Property at an Overvaluation.*

COIT v. NORTH CAROLINA GOLD AMALGAMATING CO.

1886. 119 U. S. 343, 39 L. ed. 420.¹⁰

THIS was a bill in equity against a corporation and its stockholders to enforce a debt due from the former against the latter.

MR. JUSTICE FIELD.—The defendant, the North Carolina Gold Amalgamating Company, was incorporated under the laws of North Carolina on the 30th of January, 1874, for the purpose, among other things, of working, milling, smelting, reducing and assaying ores and metals, with the power to purchase such property, real and personal, as might be necessary in its business, and to mortgage or sell the same.

The plaintiff is the holder of a judgment against the company for \$5,489, recovered in the Court of Common Pleas of Philadelphia, on the 18th of May, 1879, upon its two drafts, one dated June 1, 1874, and the other August 15, 1874, each payable four months after its date. Unable to obtain satisfaction of this judgment upon execution, and finding that the company was insolvent, the plaintiff brought this suit to compel the stockholders to pay what he claims to be due and unpaid on the shares of the capital stock held by them, alleging that he had frequently applied to the officers of the company to institute a suit for that purpose, but that under various pretenses they refused to take any action in the premises.

By its charter the minimum capital stock was fixed at \$100,000, divided into 1,000 shares of \$100 each, with power to increase it from time to time, by a majority vote of the stockholders, to two million and a half of dollars. The charter provided that the subscription to the capital stock might be paid "in such installments, in such manner and in such property, real and personal," as a majority of the corporators might determine, and that the stockholders should not be liable for any loss or damage, or be responsible beyond the assets of the Company.

* See *Runner, Assignee, v. Dwiggins* (1896) 147 Ind. 238, 46 N. E. 580, 36 L. R. A. 645; *Thompson v. Knight* (1902) 74 App. Div. (N. Y.) 316, 76 N. Y. S. 599, 11 N. Y. Ann. Cas. 278; *Flinn, Assignee, v. Bagley* (1881) 7 Fed. 785. See also article, 22 Harv. Law Rev. 319, 335-6.—Eds.

¹⁰ Portion of opinion omitted.—Eds.

Previously to the charter the corporators had been engaged in mining operations, conducting their business under the name and title which they took as a corporation. Upon obtaining the charter the capital stock was paid by the property of the former association, which was estimated to be of the value of \$100,000, the shares being divided among the stockholders in proportion to their respective interests in the property. Each stockholder placed his estimate upon the property, and the average estimate amounted to \$137,500. This sum they reduced to \$100,000, inasmuch as the capital stock was to be of that amount.

The plaintiff contends, and it is the principal basis of his suit, that the valuation thus put upon the property was illegally and fraudulently made at an amount far above its actual value, averring that the property consisted only of a machine for crushing ores, the right to use a patent called the Crosby process, and the charter of the proposed organization; that the articles had no market or actual value, and, therefore, that the capital stock issued thereon was not fully paid, or paid to any substantial extent, and that the holders thereof were still liable to the corporation and its creditors for the unpaid subscription.

If it were proved that actual fraud was committed in the payment of the stock, and that the complainant had given credit to the company from a belief that its stock was fully paid, there would undoubtedly be substantial ground for the relief asked. But where the charter authorizes capital stock to be paid in property, and the shareholders honestly and in good faith put in property instead of money, in payment of their subscriptions, third parties have no ground of complaint. The case is very different from that in which subscriptions to stock are payable in cash, and where only a part of the installments has been paid. In that case there is still a debt due to the corporation, which, if it become insolvent, may be sequestered in equity by the creditors, as a trust fund liable to the payment of their debts. But where full-paid stock is issued for property received there must be actual fraud in the transaction to enable creditors of the corporation to call the stockholders to account. A gross and obvious overvaluation of property would be strong evidence of fraud. *Boynton v. Hatch*, 47 N. Y. 225; *Van Cott v. Van Brunt*, 82 N. Y. 535; *Carr v. LeFevre*, 27 Pa. St. 413.

But the allegation of intentional and fraudulent overvaluation of the property is not sustained by the evidence. The patent and the machinery had been used by the corporators in their business, which was continued under the charter. They were immediately serviceable, and therefore had to the company a present value. The corporators may have placed too high an estimate upon the property, but the court below finds that its valuation was honestly and fairly made; and there is only one item, the value of the chartered privileges, which is at all liable to any legal objection.

But if that were deducted, the remaining amount would be so near to the aggregate capital that no implication could be raised against the entire good faith of the parties in the transaction. * * * The plaintiff had placed no reliance upon the supposed paid-up capital of the company on the increased shares, and therefore has no cause of complaint by reason of their subsequent recall. Had a new indebtedness been created by the company after the issue of the stock and before its recall, a different question would have arisen. The creditor in that case, relying on the faith of the stock being fully paid, might have insisted upon its full payment. But no such new indebtedness was created, and we think, therefore, that the stockholders cannot be called upon, at the suit of the plaintiff, to pay in the amount of the stock, which, though issued, was soon afterward recalled and canceled.

*Judgment affirmed.*¹¹

¹¹ *Oregon Gold Mining Co. v. Roper* (1892) App. Cases, 125, at page 136: "Consequently, if shares are issued against money, it appears to me that any payment to the company less than the nominal amount of the share must, by force of the statute, and notwithstanding any agreement to the contrary, be considered as a payment to account, the member remaining liable to contribute the balance, when duly called for."

"A company is free to contract with an applicant for its shares; and when he pays in cash the nominal amount of the shares allotted to him, the company may at once return the money in satisfaction of its legal indebtedness for goods supplied or services rendered by him. That circuitous process is not essential. It has been decided that, under the Act of 1862, shares may be lawfully issued as fully paid up, for considerations which the company has agreed to accept as representing in money's worth the nominal value of the shares. I do not think any other decision could have been given in the case of a genuine transaction of that nature where the consideration was the substantial equivalent of full payment of the shares in cash. The possible objection to such an arrangement is that the company may over-estimate the value of the consideration, and, therefore, receive less than nominal value for its shares. The court would doubtless refuse effect to a colourable transaction, entered into for the purpose or with the obvious result of enabling the company to issue its shares at a discount; but it has been ruled that, so long as the company honestly regards the consideration given as fairly representing the nominal value of the shares in cash, its estimate ought not be critically examined. That state of the law is certainly calculated to induce companies who are in want of money, and whose shares are unsalable except at a discount, to pay extravagant prices for goods or work to persons who are willing to take payment in shares. The rule is capable of being abused, and I have little doubt that it has been liberally construed in practice."

See *Anderson's Case*, L. R. (1877) 7 Ch. Div. 75.

Graves v. Brooks (1898) 117 Mich. 424, at page 426, 75 N. W. 932: "In order to render stock, issued as full-paid and nonassessable, assessable, it is necessary to establish either an intentional fraud in fact, or such reckless conduct in fixing the value of the property conveyed, without regard to its value, that an intent to defraud may be inferred."

See *Bostwick v. Young*, (1907) 118 App. Div. (N. Y.) 490, 103 N. Y. S. 607, Affd. 194 N. Y. 516, 87 N. E. 1115, in accord with *Van Cott v. Van Brunt*, 82 N. Y. 535.

See *Rathbone v. Ayre* (1907) 121 App. Div. (N. Y.) 355, 105 N. Y. S. 1041, where \$500,000 par value of stock was issued for property which had been bought for \$85,000 in cash. A judgment of non-suit granted by the trial justice on the ground that there was no affirmative evidence of fraudu-

STATE TRUST CO. v. TURNER.

1900. 111 Iowa 664, 82 N. W. 1029, 53 L. R. A. 136.¹²

ACTION at law to recover of defendant the amount of a judgment held by plaintiff against a corporation known as the Hess Electric Storage-Battery Company. The case was tried to the court on an agreed statement of facts, resulting in a judgment for defendant. Plaintiff appeals.—*Affirmed*.

DEEMER, J.—The Hess Electric Storage-Battery Company is a corporation organized under the laws of this state in the year 1890. It was created "to perfect a storage-battery system patented by one H. K. Hess, and to adapt it to practical use for light and power; the buying and selling of the patent and any other necessary and proper article to be used herewith; to procure other letters patent; and to buy and sell electric light plants, patents, batteries, etc.; and to lease, purchase, or sell electric current for any legitimate purpose." The capital stock was fixed at one hundred thousand dollars, divided into one thousand shares of one hundred dollars each, of which not exceeding ninety thousand dollars might be issued and used as fully paid for the purchase of patents or property to be used in the business. The balance of the stock was to remain as treasury stock, and sold to such persons and on such terms as the board of directors should determine; none of it to be issued, however, until fully paid. The articles were signed by H. C. Porter, H. K. Hess, A. R. Case, defendant, and others. Defendant was vice-president and a director of the corporation. After the filing of the articles Porter, Case, and Hess made a proposition to sell certain patents which they claimed to own and hold, to the corporation, for ninety thousand dollars of its capital stock, fully paid up, and an additional sum of five hundred dollars in cash as soon as the corporation was able to pay. The board of directors of the corporation accepted the proposition, and

lent overvaluation, was reversed by the Appellate Division, Kellogg, J. dissenting. The judgment of the Appellate Division was reversed by the Court of Appeals on the dissenting opinion of Kellogg, J., 196 N. Y. 503, 89 N. E. 1111; *Cf. Skank v. Andrews* (1874) 57 N. Y. 133, good faith rule applied. In *Lake Superior Iron Co. v. Drexel* (1882) 90 N. Y. 87, \$2,500,000 par value of stock was issued for manufacturing property and patents. *Held*, the question whether the trustees acted in good faith was a question for the jury; and that the fact that persons receiving stock agreed to turn back a portion of it, and did turn it back, is not conclusive upon the question of fraud, and that the question whether the form the transaction took was a mere sham intended as an evasion of the statute, was a question of fact for the determination of the jury. *Cf. New York cases referred to in Note 13, infra*.

In *American Tube & Iron Co. v. Baden Gas Co.*, (1895) 165 Pa. St. 489, 30 Atl. 940; \$500,000 par value of stock was issued for oil property and a part of it turned back. *Held*, there was no fraud and no liability to creditors.—Eds.

¹² Portion of opinion omitted.—Eds.

Porter, Case, and Hess made an assignment of their patents, and of such property as they had on hand for experimental and manufacturing purposes, to the corporation, and received from it ninety thousand dollars of its fully-paid stock. The books of the corporation show that the day before the aforesaid proposition was made, ten shares of stock, of the face value of one thousand dollars, were issued to defendant, Turner. This stock recited that it was fully paid. Turner paid nothing to the corporation for the stock, but the same was treated by all parties as a part of the ninety thousand dollars to be issued to Porter et al., and was issued to him on their order. He paid Porter and his associates twenty cents on the dollar in cash for the stock, and has owned the same to this day. On the day the proposition was made, twenty shares of the stock were issued to Porter; but he never received them, and the books show that they were canceled and reissued to D. H. Gouging and T. S. Catcart. Ten of these shares issued to Gouging were canceled, and new certificates for the same were issued to defendant. The other ten of these twenty shares were also canceled and reissued to defendant. Neither Turner, Gouging, nor Porter paid anything to the corporation for this stock, but it was treated as part of the ninety thousand dollars hitherto mentioned. Turner paid Gouging twenty cents on the dollar for the stock issued to him. The remainder of the ninety thousand dollars in stock was issued as follows: ten shares to R. R. Ballis, ten to F. B. Collins, ten to George C. Boggs, five to O. L. F. Browne, five to D. W. Chase, five to A. I. Lee, five to J. H. Woods, five to F. A. Fields, and five to W. H. Langan, all of whom had signed the original articles of incorporation; and the balance was issued to Porter et al., or to other persons on their order. The stockholders have never held a meeting, but the board of directors held meetings until the latter part of the year 1894, since which time it has held no meetings. It was also agreed as follows: "(6) That the chemicals, material, and property mentioned in the said written proposition, including tools and instruments intended or adapted to the manufacture of batteries and motors, or used or intended for experiment, were of the value of \$500, and at the time of the purchase of said property by the said Hess Electric Storage-Battery Company, as hereinbefore stated, the said patented articles had not been put largely into practical use, but many experiments and tests had been made with reference to its practical utility, all of which were known to the said Hess Electrical Storage-Battery Company, and its tests and experiments had shown satisfactory results; and the incorporators believed at the time of said purchase of said patent and property that the same was of very great value, and hoped and believed said Company would realize therefor and thereon largely more than the ninety thousand dollars paid therefor. (7) That the said incorporators and stockholders of said incorporation continued to experiment with and test said patented articles until late in the year 1894, receiving numerous

offers for the purchase of territory and for the placing of same in use upon cars and otherwise, many of which offers were rejected by said Hess Electric Storage-Battery Company because of the belief that said patents and the use of said patent articles were worth more than the offers made therefor, and for the use thereof; that during said period other inventions for the use and application of electricity as a motive power were discovered and invented, whereby and by reason whereof the Hess Electric Storage-Battery Company has not, so far, been able to realize revenues therefrom to any large extent,—that is to say, the said corporation has not been able to make any sales satisfactory to said company, and the said patents and property have never brought to the corporation any remuneration adequate to meet its entire expenditures." In September of the year 1893 the corporation borrowed of the Commercial Loan Association the sum of six hundred and seventy dollars, and executed its notes therefor, due one month after date. The loan association had knowledge of all the facts hitherto recited regarding the organization of the corporation, and of the manner in which it had issued and disposed of its stock, and was fully cognizant of all the facts regarding the purchase and sale of the patents and property, and of the value thereof. After maturity of the note, the loan association transferred the same to plaintiff. Plaintiff recovered judgment thereon against the corporation, and after an execution had been issued, and returned "No property found," it commenced this action. On these facts the case was tried to the court, resulting in a judgment for defendant, and from that judgment the appeal is taken.

Involved primarily is the so-called "trust-fund doctrine," as applied to stockholders' obligations to creditors. This is founded on the proposition that as the state undertakes to relieve the stockholder in a corporation of a general liability for the debts of the concern, to the amount that he has invested in the enterprise, he ought, in good faith, to pay in money or its equivalent the face value of the stock received; and, if he fails to do this, he should be treated as holding the remainder in trust for the benefit of the creditors of the corporation. From this proposition two apparently conflicting and inconsistent rules have grown up, one of which may be called the "true-value rule," and the other the "good-faith rule." Courts adopting the good-faith rule are also divided on the proposition as to what is necessary to be shown to constitute good faith. Some of them hold that, in the absence of an affirmative showing of fraud *aliunde*, mere overvaluation of the property given in exchange for stock will not render the stockholder liable for the difference, while others hold that overvaluation itself, especially if gross, constitutes, or at least raises a strong presumption of fraud. The development of the trust-fund doctrine may be gathered from a reading of the following: (reference to authorities omitted). It will be noticed that there is some confusion in the New York and United States

supreme court cases, and it is difficult to say just what rule prevails in Illinois. See *Sprague v. Bank*, 172 Ill. 149 (50 N. E. Rep. 19, 42 L. R. A. 606). But the supreme court of the United States has never departed from the principles of *Sawyer v. Hoag*, and other like cases. See *Camden v. Stuart*, 144 U. S. 104 (12 Sup. Ct. Rep. 585, 36 L. ed. 363).

We think our previous cases adopt the true-value rule,—perhaps not to its full extent; but such has been the drift of these cases. (The learned Judge, after referring to several cases, proceeded.) From this review it is apparent that we have, in effect, adopted the true-value rule, although saying in some cases that the reason for so doing was to prevent fraud. There is nothing in these decisions or in the statutes that inhibits the taking of property in exchange for stock, providing it is taken at its true value; and this value we do not think should in all instances, if in any, be measured by results. The parties have the right in good faith to agree on the value of the property taken, but this should not be a speculative or fictitious one. An honest mistake in judgment will not necessarily destroy the value agreed upon, but it must be such a valuation as a prudent and sensible business man would approve. Values based on visionary or speculative hopes, unwarranted by existing conditions or facts, and without reasonable evidence from present appearances, are not such as the law will tolerate, as against creditors. It is apparent that the patent and property sold the corporation by *Porter et al.*, had no such value as the parties placed upon it. They say they hoped and believed the company would realize therefor and thereon more than ninety thousand dollars, but no one had the temerity to say that he regarded the patent and property as of that value. The actual value received was but little over five hundred dollars.

But it is said that, as plaintiff's assignor had full knowledge and notice of all the facts, plaintiff cannot recover. This contention requires a little further examination of the rationale of the trust-fund doctrine. * * * In *Upton v. Tribilcock*, 91 U. S. 45, 23 L. ed. 203, this rule is announced: "The capital stock of a moneyed corporation is a fund for the payment of its debts. It is a trust fund, of which the directors are the trustees. * * * The capital stock paid in and promised to be paid in, is a fund which the trustees cannot squander or give away." Justice Woods, in *Scovill v. Thayer*, 105 U. S. 143 (26 L. ed. 968), says: "The reason is that the stock subscribed is considered in equity as a trust fund for the payment of creditors. It is so held out to the public, who have no means of knowing the private contracts made between the corporation and its stockholders. The creditor, therefore, has the right to presume that the stock subscribed has been paid or will be paid up; and if it is not, a court of equity will, at his instance require it to be paid." * * * Following this doctrine to its logical conclusion, it was held in *Bank v. Alden*, 129 U. S. 372 (9 Sup. Ct. Rep.

332, 32 L. ed. 725), that, where the creditor has full knowledge of the transaction between the corporation and its stockholder at the time he extends credit, he cannot be heard to complain, for the reason that no credit is given upon a representation of a different set of facts than those which actually existed. See, also (reference to authorities omitted). Indeed, we find no case to the contrary, unless it be *Sprague v. Bank*, 172 Ill. 149 (50 N. E. Rep. 19, 42 L. R. A. 606). That decision was based on a statute, however, which is somewhat different from ours, in that it made each stockholder liable for the debts of the corporation to the extent of the amount that may be unpaid on the stock held by him. Our statute says that nothing in the chapter contained, and nothing in the articles of incorporation, shall relieve the stockholders from individual liability, etc. (Code, section 1631); leaving the liability to be determined under the general law. *Light Co. v. Child*, 68 Conn. 522 (37 Atl. Rep. 391), relied on by appellant, is not in point. There the statute imposed a liability on the stockholder to the extent of twenty-five per cent. of the amount of stock held by him. We have heretofore recognized these rules. While saying *arguendo* that a sale of stock at a less rate than that fixed in the charter is a fraud upon the law and the stockholders *Olipphant v. Mining Co.* (63 Iowa 332) yet in *Goff v. Windmill Co.* (62 Iowa 691), we further said: "The public has a right to assume, when the stock of a company has been issued as full-paid stock, that it has been paid for in money, or in property at a fair value. * * * If it has not been paid, * * * while this might be ground for a proceeding in the interest of the public to wind up the company, it is not ground on which the plaintiff can predicate his right to relief; * * * and, besides, he not only knew upon what basis the stock had been subscribed and paid for, but he subscribed and paid for his stock on the same basis." This, it will be observed, was also *dictum*. But in *Callanan v. Windsor*, 78 Iowa 193, we held, in effect, that the assignee of a creditor of a corporation could not recover unpaid subscriptions to capital stock where the creditor knew when he extended credit that the stock, although issued as fully paid, had not in fact been so paid. Referring to the statute (Code 1873, section 1082), which is the same as section 1631 of the present Code, we said: "We are aware of the provisions of section 1082 of the Code. The primary object of those provisions was to protect creditors of the company. They should not be held to apply to a case of this kind, where, by virtue of a valid agreement, to which the original creditor was a party, nothing was due or collectible on the stock of the stockholder." In that case we approved the doctrine of *Scovill v. Thayer* (105 U. S. 143) and *Robinson v. Bedwell*, (22 Cal. 379). In *Stout v. Hubbell* (104 Iowa 499), the same rule is recognized and applied; but, as plaintiff in that case had no notice, he was permitted to recover. See, also, *Clark v. Coal Co.*, 86 Iowa 436. As the Commercial Loan Association had full knowledge of all the facts relating to the is-

suance and payment for the stock owned by the defendant, it could not recover. Does plaintiff, its transferee after maturity, have any greater rights? We think not. Our conclusion is that the judgment of the trial court should be, and it is,

*Affirmed.*¹²

B—BY STATUTE. STATUTORY LIABILITY OF STOCKHOLDERS TO CREDITORS.

CHRISTOPHER v. NORVELL.

1905. 201 U. S. 216, 50 L. ed. 732, 26 Sup. Ct. 502.

THE facts, which involve the right of a receiver of a national bank in Florida to enforce the statutory liability under §5151, Rev. Stat., against a married woman, a resident of that State and owner of record of shares of stock of the bank, are stated in the opinion.

MR. JUSTICE HARLAN delivered the opinion of the court.

By the Revised Statutes of the United States it is provided that the shareholders of every national banking association shall be held individually responsible, equally and ratably, and not one for another, for all contracts, debts, and engagements of such association, to the extent of the amount of their stock therein, at the par value

¹² *Sprague v. National Bank of America* (1898) 172 Ill. 149, 50 N. E. 19, 42 L. R. A. 606, 64 Am. St. 17; *Held*, that the holder of watered stock is liable also to creditors who extended credit with knowledge that the stock was watered.

Gillette v. Chicago Title & Trust Co. (1907) 230 Ill. 373, 82 N. E. 891; *Held*, that property must be taken at its fair cash market value, or if it has no ascertainable market value, only at such price as might be realized by selling the property to others for cash.

Esgen v. Smith (1901) 113 Iowa 25, at p. 28, 84 N. W. 635: "It is sufficient to say that, whatever rule may be adopted, be it the true-value or good faith one, it is a rule for the benefit of creditors, and not for the advantage of stockholders."

Van Cleve v. Berkey (1898) 143 Mo. 109, 44 S. W. 743, 42 L. R. A. 593; full review of the authorities; fair value rule applied.

Hobgood v. Ehlen (1906) 141 N. C. 344, 53 S. E. 857; *Held*, that a margin may be allowed for an honest difference of opinion, but a valuation grossly excessive and knowingly made is a fraud on creditors.

Boynton v. Andrews (1875) 63 N. Y. 93. *Held*, that in the case of property, the value of which is well known and understood, or capable of being easily ascertained, the purchase of it at a price far beyond its real value, raises a strong presumption of fraud.

Douglas v. Ireland (1878) 73 N. Y. 100. *Held*, that to prove fraud it is sufficient to show (1) that the stock exceeded in amount the value of the property, and (2) that the trustees issued it deliberately and with knowledge of the real value.

National Tube Works Co. v. Gilfillan (1891) 124 N. Y. 302, 26 N. E. 538; *Held*, that it is not necessary to prove fraudulent intent.

See also *Stevens v. Episcopal Church History Co.* (1910) 140 App. Div. (N. Y.) 570, 125 N. Y. S. 573; as to whether an executory contract for future services in writing and editing a book is property for which stock may be

thereof, in addition to the amount invested in such shares; that persons holding stock as executors, administrators, guardians or trustees, shall not be personally subject to any liabilities as stockholders, the estates and funds in their hands being liable in like manner and to the same extent as the testator, intestate, ward, or person interested in such trust funds would be if living and competent to act and hold the stock in his own name; and, that a receiver of a national bank may, if necessary to pay the debts of such association, enforce the individual liability of the stockholders. Rev. Stat. §§ 5151, 5152, 5234.

Proceeding under these statutes the receiver of the First National Bank of Florida brought this action against Henrietta S. Christopher (her husband John G. Christopher being joined as co-defendant) to recover the amount due from her as a shareholder of that bank under an assessment made by the Comptroller of the Currency against the stockholders of that bank in order to pay its debts.

Did the coverture of Mrs. Christopher at the time her name was placed on the books of the bank as a shareholder as well as when she received the certificate of stock, protect her against a *personal* judgment at law for the amount due under the assessment made by the Comptroller of the Currency? That is the controlling question in the case.

This question is, we think, substantially answered by the judgment of this court in *Keyser v. Hitz*, 133 U. S. 138, 150, 152. That was an action at law against Mrs. Hitz, a married woman, who owned shares of stock in a savings bank which was converted into a national bank. The action against her was based on an assessment made by the Comptroller of the Currency. One of the contentions in the case was that the coverture of the defendant at the time she acquired the stock, as well as when the bank failed, protected her against an assessment under the act of Congress. The transaction occurred in the District of Columbia, where the bank was located. It was not contended that the defendant was incapacitated by the laws of the District from becoming the owner of bank stock, and hence the court did not consider what would have been the result, if the local statutes had prohibited married women from becoming the owners of bank stock. Upon that basis, the court said: "Assuming then, that she was not incapacitated from becoming the owner of stock in a bank, and that she was a shareholder in the savings bank, she became, upon the conversion of that bank into a national bank, a shareholder in the latter. Rev. Stat., § 5154. In that event she became, *by force of the statute*, individually responsible to the amount of her stock, at the par value thereof, for the contracts, debts and engagements of the national bank equally and ratably

issued; *Camden v. Stewart* (1892) 144 U. S. 104, 36 L. ed. 363, 12 Sup. Ct. 585 and *Washburn v. Nat. Wall-Paper Co.* (1897) 81 Fed. 17, 26 C. C. A. 312, as to whether stock may be issued in payment for good-will. See article in 22 *Harvard Law Review* 319-339, by George W. Wickersham.—Eds.

with other shareholders. Section 5151, which imposes such individual responsibility upon the shareholders of national banks, makes no exception in favor of married women. The only persons holding shares of national bank stock, whom the statute exempts from this personal responsibility, are executors, administrators, guardians, or trustees. Section 5152. It is not for the courts, by mere construction, to recognize an exemption which Congress has not given." Again: "We are of the opinion that the coverture of the defendant did not prevent the plaintiff from recovering a judgment against her for the amount of the assessment in question, if she was, *within the meaning of the statute*, a shareholder in the bank at the time of its suspension. But the question as to what property may be reached in the enforcement of such judgment is not before us, and we express no opinion upon it."

The argument is that at common law a married woman could not make, or bind herself personally by, a contract, and was incapable, by the law of Florida, as at common law, of entering into a contract, at least one that would subject her to personal liability; that the relation of a shareholder to a national banking association was of a contractual character; and consequently, to render a personal judgment against the defendant Mrs. Christopher was, in effect, to hold her personally bound by a contract which under the laws of Florida she was incapable of making.

The vice in this argument is in the assumption that the liability of Mrs. Christopher as a shareholder arises *wholly* out of *contract* between herself and the bank or its creditors; whereas, upon becoming a shareholder, she made, strictly, no direct contract with anyone, and became, as was held in *Keyser v. Hitz*, above cited, *by force of the statute* individually responsible to the amount of her stock, for the contracts, debts and engagements of the bank equally and ratably with other shareholders. Such statutory liability was created for the protection of creditors, and in order to strengthen the bank in the confidence of the public. The bank, although its shares of stock were private property, was an instrumentality of the general government in the conduct of its affairs. *Farmers' &c. Nat. Bank v. Dearing*, 91 U. S. 29, 33. In *Davis v. Elmira Savings Bank*, 161 U. S. 275, 283, the court said that "national banks are instrumentalities of the Federal government created for public purposes, and as such are necessarily subject to the paramount authority of the United States." This principle was reaffirmed in *Easton v. Iowa*, 188 U. S. 220, 237. See, also, *Pacific Nat. Bank v. Mixter*, 124 U. S. 721.

In *McClaine v. Rankin*, 197 U. S. 154, 161, 163, which was an action against a shareholder of a national bank to recover the amount due on an assessment made by the Comptroller of the Currency, and in which the question was as to the nature of the cause of action, this court said: "Some statutes imposing individual liability are merely in affirmation of the common law, while others impose

an individual liability other than that at common law. If § 5151 had provided that subscribing to stock or taking shares of stock amounted to a promise directly to every creditor, then that liability would have been a liability by contract. But the words of § 5151 do not mean that the stockholder promises the creditor as surety for the debts of the corporation, but merely impose a liability on him as secondary to those debts, which debts remain distinct, and to which the stockholder is not a party. The liability is a consequence of the breach by the corporation of *its* contract to pay, and is collateral and *statutory*. . . . But here the right to sue did not obtain until the Comptroller of the Currency had acted, and his order was *the basis of the suit*. The statute of limitations did not commence to run until assessment made, and then it ran as against an action *to enforce the statutory liability*, and not an action for breach of contract."

In *Robinson v. Turrentine*, 59 Fed. Rep. 554, 555, it was held that the liability of a married woman for an assessment upon national bank stock did not grow out of contract, although it was one of a class of liabilities which may be enforced by an action in form *ex contractu*. In the same case it was said: "By the banking laws of the United States all the shares in the stock of national banks are liable to an assessment like the one levied on the stock of plaintiff's bank. To hold that a state law, were there such a law, could except certain shares from liability, would enable States to defeat the policy of the Federal Government in establishing the national banking system. That the Congress has power to establish and legislate for such banks has not, since 1819, been an open question. *McCulloch v. Maryland*, 4 Wheat. 316. If a purchase of stocks in a national bank by a married woman without the written consent of her husband gives her the ownership of such stock, judgment must be given against the *feme* defendant. If she owned the stock at the failure of the bank, she is liable to the assessment; if she did not, she is not liable. While the Federal Government exclusively controls the question of the liabilities of stockholders in national banks, it is not doubted but that a State has power to say that, for reasons seeming good to its legislature, and not in conflict with organic law, a particular class of persons shall not be permitted to own particular classes of property."

In *Kerr v. Urie*, 86 Maryland, 72, 77, it was held that a married woman residing in Maryland was capable of holding shares of stock in a national bank located in Texas, and, as such shareholder, was subject to the personal liability imposed by the national banking laws, without regard to the question whether she was entitled under the laws of the State where the bank was located to become the owner of such stock. The court said: "We conclude, therefore, that by virtue of the transfer in Maryland, and without regard to the laws of Texas, Mrs. Urie became the equitable and real owner of the stock in question, and if this be so, no question as to her powers of disposi-

tion, or as to whether she is or is not capable under the laws of Texas to make contracts, can arise in this case, for the liability of the stockholder arises not under any law of Texas, which it is contended has not been proven in this case, but under the act of Congress. And the contracts which it is claimed she is liable on are not her contracts, but the contracts of the bank. *Witters v. Sowles*, 35 Fed. Rep. 641; § 5152, Rev. Stat. The right to be a stockholder is given to her by the law of the State where she resides, and her rights *and liabilities* as such are provided *by the acts of Congress.*"

Recurring to the provisions in the statute and constitution of Florida, it is clear that they do not incapacitate a married woman in that State from becoming the owner by bequest or otherwise of stock in a national banking association. On the contrary, it seems that all property, real and personal, owned by a married woman before marriage, or lawfully acquired afterward by gift, devise, bequest, descent or purchase, is her separate property. Nevertheless, it is said, by the settled course of decisions in that State a married woman cannot bind herself personally by contract at law or in equity, or by becoming a partner, or by making a promissory note. *Dollner v. Snow*, 16 Florida, 86; *Hodges v. Price*, 18 Florida, 342; *Goss v. Furman*, 21 Florida, 406; *De Graum v. Jones*, 23 Florida, 83, and *Randall v. Bourgardez*, 23 Florida, 264. But those cases are not in point here; for, in each of them, the personal liability attempted to be imposed upon the married woman arose *entirely* out of contract, express or implied, on her part, and not by force of any statute. The argument made in this case in behalf of Mrs. Christopher assumes that the liability sought to be fastened upon her arises wholly out of contract; that is, out of an implied obligation, at the time her name was placed on the registry of shares and she received dividends, to contribute to the extent of the value of such shares to the payment of the debts of the bank. But that implied obligation, although contractual in its nature, could not, standing alone, be made the basis of this action. Without the statute she could not be made liable individually for the debts of the bank at all. No implied obligation to contribute to the payment of such debts could arise from the single fact that she became and was a shareholder. Her liability for the debts of the bank is created by the statute, although in a limited sense there is an element of contract in her having become a shareholder; and the right of the receiver to maintain this action depends upon, and has its sanction in, the statute creating liability against each shareholder, in whatever way he may have become such. There have been cases in which there appeared such elements of contract as were deemed sufficient, in particular circumstances, to support an action. *Concord First Nat. Bank v. Hawkins*, 174 U. S. 364, 372; *Whitman v. Oxford Nat. Bank*, 176 U. S. 559, 565, 566; *Matteson v. Dent*, 176 U. S. 521. But that fact does not justify the contention that an action upon an assessment made by the Comptroller is not based upon the statute.

In *McDonald v. Thompson*, 184 U. S. 71, 73, which was the case of a formal subscription to the capital stock of a national bank, and which also involved the meaning of the words "contract or promise in writing" in a statute of limitations, the court said: "There was no contract in writing with the creditors or depositors of the bank, and none with the bank itself, to which the receiver could be said to be a privy, except to pay for the stock as originally issued. Granting there was a contract with the creditors to pay a sum equal to the value of the stock taken, in addition to the sum invested in the shares, this was a contract created by the statute, and obligatory upon the stockholders by reason of the statute existing at the time of their subscription; but it was not a contract in writing within the meaning of the Nebraska act (of limitation), since the writing—that is, the subscription—contained no reference whatever to the statutory obligation, and no promise to respond beyond the amount of the subscription. In none of the numerous cases upon the subject in this court is this obligation treated as an express contract, but as one created by the statute and implied from the express contract of the stockholders to take and pay for shares in the association." All shareholders of stock in national banks become such, subject to the condition, declared by statute, that liability, to the extent of their shares, is imposed upon them for the contracts, debts and engagements of the bank. The statute, in effect, says to all who become owners of national bank stock, no matter in what way they become shareholders, that they cannot enjoy the benefits accruing to shareholders, and escape liability for the contracts, debts and engagements of the bank. In other words, the Government that created the bank has prescribed the terms upon which ownership of its shares could be acquired, and individual liability incurred by shareholders—executors, administrators, guardians or trustees only being exempted from individual liability. No exception is made in favor of married women holding property. If the constitution or statutes of Florida had expressly incapacitated or forbidden a married woman from becoming under any circumstances the owner of bank shares—as counsel for plaintiff in error insists is the case—a question would be presented that does not arise upon the record of this case; and as the local law does not forbid married women from becoming the owners of bank stock, we do not go beyond what is necessary for the decision of the present case under the national banking law. All that we now decide is that the court below properly interpreted the statute, and did not err in rendering a personal judgment against Mrs. Christopher, as a shareholder in the bank, for the amount due under the assessment of the Comptroller. In

what way the plaintiff may proceed in order to obtain satisfaction of the judgment is not a question to be determined in this action.

Judgment affirmed.

MR. JUSTICE WHITE and MR. JUSTICE McKENNA concur in the result.¹⁴

¹⁴ *McClaine v. Rankin* (1904) 197 U. S. 154 at p. 159, 49 L. ed. 705, 25 Sup. Ct. 410: "Conceding that a statutory liability may be contractual in its nature, or more accurately, quasi-contractual, does it follow that an action given by statute should be regarded as brought on simple contract, or for breach of a simple contract, and, therefore, as coming within the provision in question?"

Bernheimer v. Converse (1906) 206 U. S., 516 at pp. 532-533, 51 L. ed. 1163, at p. 1175, 27 Sup. Ct. 755: "Nor can we see any substantial difference in this respect between a liability to be ascertained for the benefit of creditors upon a stock subscription and the liability for the same purpose which is entailed by becoming a member of a corporation through the purchase of stock whereby a contract is implied in favor of creditors. The object of the enforcement of both liabilities is for the benefit of creditors, and while it is true that one promise is directly to the corporation and the other does not belong to the corporation but is for the benefit of its creditors, either liability may be enforced through a receiver acting for the benefit of creditors under the orders of a court in winding up the corporation in case of its insolvency." Cf. *Mfg's. Commercial Company v. Heckscher* (1911) 144 App. Div. (N. Y.) 600, 129 N. Y. S. 556;

Cochran v. Wiechers, (1890) 119 N. Y. 399, 23 N. E. 803, 7 L. R. A. 553; *Held*, that the liability of the stockholder is in the nature of a contract obligation and survives the death of the stockholder and continues against the executors. "It is not like the liability of a trustee for neglecting to make a report or for declaring dividends out of the capital stock, or acts of a kindred character. These are breaches of a statute on the part of the managing agents of the corporation for which the statute has made them liable and this liability cannot be said to rest upon or grow out of a contract. The liability of a stockholder in the present case is different. Upon becoming the owner of the stock, he voluntarily assumes the obligations imposed by the statute and the creditors of the corporation who trust it may be said to do so upon the faith of the statute, which is part of the contract. The statutory obligation is inherent in and forms a part of every contract that a corporation makes with creditors prior to the time that the certificate required by the statute is filed."

As to the statutory liability of stockholders, what obligations it covers, when it accrues, when it is barred by the statute of limitations, who are the proper parties to sue or to be sued, whether the creditor may sue for himself alone or must sue on behalf of all the other creditors, whether he may sue at law or in equity, these are all questions depending primarily for their determination upon the particular language of the statute imposing the liability. See *Terry v. Little* (1879) 101 U. S. 216 at page 218, 25 L. ed. 864 at p. 865, *Fourth National Bank of New York v. Francklyn* (1887) 120 U. S. 747, 30 L. ed. 825, 7 Sup. Ct. 757; *Hirshfeld v. Fitzgerald* (1898) 157 N. Y., 166, 50 N. E. 997, 46 L. R. A. 839; *Lang v. Lutz* (1905) 180 N. Y., 254, 73 N. E. 24; *Rider v. Fritchey* (1892) 49 Ohio St. 285, 30 N. E. 692, 15 L. R. A. 513; *Wing v. Slater* (1896) 19 R. I. 597, 35 Atl. 302, 33 L. R. A. 566;

Ward v. Joslin (1901) 186 U. S., 142, 46 L. ed. 1093, 22 Sup. Ct. 807; *held*, in case of a creditor who had recovered a judgment by default against a Kansas corporation on an ultra vires contract, that the liability of a stockholder does not extend to obligations incurred as a result of an ultra vires transaction. See *Close v. Potter* (1898) 155 N. Y., 145 at p. 157, 49 N. E. 686; *Leighton v. Leighton Lee Association* (1911) 146 App. Div. (N. Y.) 255, 130 N. Y. S. 935.—Eds.

PINNEY v. NELSON.

1901. 183 U. S. 144, 46 L. ed. 125, 22 Sup. Ct. 52.¹⁵

THIS was an action to enforce a personal liability of stockholders. It was commenced in a justice's court of Los Angeles city, Los Angeles County, California, on September 30, 1898, by the defendant in error against the plaintiffs in error. It was subsequently transferred to the superior court of the county, where a trial was had on January 17, 1900, before the court without a jury. A stipulation was signed as to the truth of various averments in the complaint and answer, which concluded as follows:

"And it is stipulated that the only question in this case is as to whether section 322 of the Civil Code of California is in violation of the provisions of the Constitution of the United States, and if it is in violation of such provisions defendants are entitled to judgment, but if said section is not in violation of said provisions, then plaintiff is entitled to judgment as prayed for in his complaint."

Findings of fact were also made, among which were the following: (1) That the company was created for the purpose of carrying on business in California; (2) That the defendants are and were at all times herein mentioned residents and citizens of the State of California; (3) That the indebtedness was created by contracts made, executed and to be performed in the state of California.

Article 12, section 15, of the constitution of California, adopted in 1879, reads:

"No corporation organized outside the limits of this State shall be allowed to transact business within this State on more favorable conditions than are prescribed by law to similar corporations organized under the laws of this State."

Section 322 of the Civil Code of California, as amended March 15, 1876, provides as follows:

"Each stockholder of a corporation is individually and personally liable for such proportion of its debts and liabilities as the amount of stock or shares owned by him bears to the whole of the subscribed capital stock or shares of the corporation, and for a like proportion only of each debt or claim against the corporation. Any creditor of the corporation may institute joint or several actions against any of its stockholders, for the proportion of his claim payable by each, and in such action the court must ascertain the proportion of the claim or debt for which each defendant is liable, and a several judgment must be rendered against each, in conformity therewith.

"The liability of each stockholder of a corporation, formed under the laws of any other State or Territory of the United States, or of any foreign country, and doing business within this State, shall be the same as the liability of a stockholder of a corporation created under the constitution and laws of this State."

¹⁵ Statement abridged.—Eds.

By the stipulation above referred to the truthfulness of the following averment in the answer was admitted:

"Defendants allege that there is no statute of the State of Colorado providing that stockholders shall be liable for any portion of the indebtedness of a corporation, and allege that under the laws of the State of Colorado a stockholder in a corporation is not liable for any portion of the indebtedness of said corporation."

MR. JUSTICE BREWER delivered the opinion of the court.

The plaintiffs in error rely upon the proposition that the liability of a stockholder is determined by the charter of the corporation and the laws of the State in which the incorporation is had. "If the constitution to which a corporation has agreed does *not* provide for individual liability to creditors, he cannot be charged with individual liability anywhere. (Morawetz on Corporations, 2d ed. sec. 874.)" They invoke the *lex loci contractus*, and say that the stockholders' contract was made in Colorado, that being the State in which the Los Angeles Iron and Steel Company was incorporated; that by the laws of that State there is no personal liability of stockholders; that it is not within the power of California to change the terms of that contract, the Federal Constitution (Art. I, sec. 10) forbidding a State to pass a law impairing the obligation of contracts; that while California, which prescribes an individual liability of stockholders, may if it sees fit exclude every corporation of another State whose stockholders do not assent to such liability, yet if it fails to do so, and such Colorado corporation actually comes into California to transact business, such coming into the State and the transaction of business therein do not change the terms of the stockholders' contracts, or impose a personal liability; and also that in such a case an attempt to enforce the statutory provisions of California so far as to change the personal liability of incorporators in the foreign corporation, is in conflict with the due process and equal protection clauses of the first section of the Fourteenth Amendment.

With reference to the contention that the law of California impairs the obligation of the contract of the stockholders, it is enough to say that that law, both constitutional and statutory, was enacted long before the incorporation of the Los Angeles Iron and Steel Company, and that therefore section 10 of Article I of the Federal Constitution has no application. "It is equally clear that the law of the State to which the Constitution refers in that clause must be one enacted after the making of the contract, the obligation of which is claimed to be impaired." *Lehigh Water Co. v. Easton*, 121 U. S. 388, 391. See also, *Central Land Co. v. Laidley*, 159 U. S. 103, 111; *McCullough v. Virginia*, 172 U. S. 102, 116.

Passing to a consideration of the stockholders' contract in the light of the other contention, it may be said that ordinarily it is controlled by the law of the State in which the incorporation is had. That is the place of contract, and generally, the law of the place where a contract is made governs its nature, interpretation and obligation.

While this is so, it is also true that parties in making a contract may have in view some other law than that of the place, and when that is so that other law will control. That the parties have some other law in view and contract with reference to it is shown by an express declaration to that effect. In the absence of such declaration it may be disclosed by the terms of the contract and the purpose with which it is entered into. In *Pritchard v. Norton*, 106 U. S. 124, many cases were cited by Mr. Justice Matthews, delivering the opinion of the court, in which these propositions were illustrated and enforced, and on page 136 it was said:

"The law we are in search of, which is to decide upon the nature, interpretation and validity of the engagement in question, is that which the parties have, either expressly or presumptively, incorporated into their contract as constituting its obligation. It has never been better described than it was incidentally by Mr. Chief Justice Marshall, in *Wayman v. Southard*, 10 Wheat. 1, 48, where he defined it as a principle of universal law, 'The principle that in every forum a contract is governed by the law with a view to which it was made.' The same idea had been expressed by Lord Mansfield in *Robinson v. Bland*, 2 Burr. 1077, 1078, 'the law of the place,' he said, 'can never be the rule where the transaction is entered into with *an express* view to the law of another country, as the rule by which it is to be governed.' And in *Lloyd v. Guibert*, Law Rep. 1 Q. B. 115, 120, in the Court of Exchequer Chamber, it was said that 'it is necessary to consider by what general law the parties intended that the transaction should be governed, or rather, by what general law it is just to presume that they have submitted themselves in the matter.' *Le Breton v. Miles*, 8 Paige (N. Y.), 261."

The subject was also discussed at length by Mr. Justice Gray in *Liverpool Steam Company v. Phenix Insurance Company*, 129 U. S. 397. In *Coghlan v. South Carolina Railroad Company*, 142 U. S. 101, 110, Mr. Justice Harlan, referring to these two opinions, observed: "The elaborate and careful review of the adjudged cases, American and English, in the two cases last cited, leaves nothing to be said upon the general subject."

In *Bank of Augusta v. Earle*, 13 Pet. 519, 588, Chief Justice Taney said:

"It is very true that a corporation can have no legal existence out of the boundaries of the sovereignty by which it is created But although it must live and have its being in that State only, yet it does not by any means follow that its existence there will not be recognized in other places; and its residence in one State creates no insuperable objection to its power of contracting in another. It is indeed a mere artificial being, invisible and intangible, yet it is a person for certain purposes in contemplation of law, and has been recognized as such by the decisions of this court. It was so held in the case of *The United States v. Amedy*, 11 Wheat. 412, and in *Beaston v. The Farmers' Bank of Delaware*, 12 Pet. 135. Now nat-

ural persons, through the intervention of agents, are continually making contracts in countries in which they do not reside, and where they are not personally present when the contract is made, and nobody has ever doubted the validity of these agreements. And what greater objection can there be to the capacity of an artificial person, by its agents, to make a contract within the scope of its limited powers, in a sovereignty in which it does not reside, provided such contracts are permitted to be made by them by the laws of the place?"

And then, after discussing the question of comity, added (p. 589) : "Adopting, as we do, the principle here stated, we proceed to inquire whether, by the comity of nations, foreign corporations are permitted to make contracts within their jurisdiction, and we can perceive no sufficient reason for excluding them when they are not contrary to the known policy of the State, or injurious to its interests.

"It is nothing more than the admission of the existence of an artificial person created by the law of another State, and clothed with the power of making certain contracts. It is but the usual comity of recognizing the law of another State."

As then a corporation can have no legal existence outside of the State in which it is incorporated, the contract of the stockholders with one another by which the corporation is created, is presumed to have been made with reference to the laws of that State, nothing being said in the charter to the contrary. But as comity permits a corporation to enter another State and do business therein, it is competent for the stockholders in making their charter to contract with reference to the laws of a State in which they propose the corporation shall do business. And in this case the stockholders in their charter specified that the purpose of the incorporation was partly business beyond the limits of Colorado, and that the principal part of such outside business should be carried on in California. Not content to rely upon the general authority which by the rules of comity the Colorado corporation would have to enter California, and transact business therein, they in terms set forth that a part of the purpose of the incorporation was the transaction of business by the corporation in California. Now when they in terms specified that they were framing a corporation for the purpose of having that corporation do business in California is it not clear that they were contracting with reference to the laws of that State? Contracting with reference to the laws of that State they must be assumed to know the provisions of those laws; that by them a personal liability was cast upon the stockholders in corporations formed under the laws of the State, and that that same liability was also imposed upon the stockholders of corporations formed under the laws of other States, and doing business within California. How can it be said that those laws do not enter into the contract and control as to all business done in pursuance of that contract within the limits of California? Suppose these same stockholders in Colorado had formed a partnership

with the expressed intent of carrying on business in California, would not that expressed intent be a clear reference to the laws of California and an incorporation of those laws into the liabilities created by the partnership business in California? And if this rule obtains as to contracts of partners between themselves, why not also as to contracts of stockholders between themselves in forming a corporation?

In this case it appears that the business transactions out of which these liabilities arose were carried on in California. They resulted from business done in California by virtue of an express contract made by the stockholders with reference to such business. It is unnecessary to express an opinion upon the question whether any personal liability would be assumed by the stockholders in reference to business transacted in Colorado. Parties may contract with special reference to carrying on business in separate States, and when they make an express contract therefor the business transacted in each of the States will be affected by the laws of those States, and may result in a difference of liability. Neither is it necessary to express any opinion upon the question whether the defendants could have been held liable under the California statutes, independently of the provisions of the Colorado charter. All that we here hold is that when a corporation is formed in one State, and by the express terms of its charter it is created for doing business in another State, and business is done in that State, it must be assumed that the charter contract was made with reference to its laws; and the liabilities which those laws impose will attend the transaction of such business.

The judgment of the Superior Court is *affirmed*.¹⁶

RISDON IRON AND LOCOMOTIVE WORKS v. FURNESS.

1905. L. R. (1906) 1 K. B. 49.¹⁷

APPEAL from a judgment of Kennedy J. on the argument of a point of law raised on pleadings, reported (1905) 1 K. B. 304.

The allegations of the statement of claim were to the following effect:—

The plaintiffs are a corporation incorporated under the laws of the State of California, in the United States of America, and carry on the business of general machinery manufacturers in that State.

The defendant is a shareholder in a company called the "Copper King, Limited," whose registered offices are in the city of London, and was at all material times the holder of shares in the company.

The Copper King, Limited, was registered as a joint stock com-

¹⁶ See *Peck v. Noe* (1908) 154 Cal. 351.—Eds.

¹⁷ Portion of statement omitted. Opinions of Romer L. J. and Mathew L. J. omitted.—Eds.

pany under the Companies Acts, 1862-1898, with a capital divided into shares of £1 each, all of which was fully subscribed, and by its memorandum of association the objects for which the company was incorporated were (*inter alia*):—

To acquire any copper or other mines in the United States of America, Australia, and elsewhere;

To search for, crush, win, get, and prepare for market ore and mineral substances of all kinds;

To purchase machinery and materials of every kind requisite for the purposes of the company;

To carry out all or any of the foregoing objects in any parts of the world either as principals or agents;

To do all other things incidental or conducive to the attainment of the above objects.

Under the articles of association the directors were empowered by art. 87 (L) to "do all such other things and take such steps as may be now or at any time become necessary so as to comply with any statutory enactment, rule, or regulation in any country, colony, or place where the company may carry on business, or where all or any part of the property and undertaking of the company may be situate."

Pursuant to the terms of the memorandum and articles of association, and until its bankruptcy and winding-up hereinafter specified, the Copper King, Limited, carried on business in the State of California.

Between September 30 and December 15, 1902, the plaintiffs, in accordance with contracts made by and between themselves and the Copper King, Limited, supplied and delivered machinery and goods to and did certain work and labour for the Copper King, Limited, at the price of \$10,404.96. The Copper King, Limited, failed to pay the plaintiffs the said sum or any part thereof, and on February 4, 1903, the plaintiffs commenced an action against the Copper King, Limited, in the Superior Court of the city and county of San Francisco, in the United States of America, for the said sum. Before this action was tried, the company was adjudicated bankrupt according to the laws of the United States.

Subsequently the shareholders passed a resolution that the company should be voluntarily wound up.

At the hearing judgment was given for the defendant. 1 K. B. (1905) 304. The plaintiffs appealed.

COLLINS M. R. This is an appeal from a judgment of Kennedy J. upon what is the modern substitute for a demurrer, and a question of law has to be decided before the facts of the case are definitely ascertained. We have, therefore, to decide the point upon the facts as they are stated in the pleadings. It appears that the defendant was a member of a limited company registered under the Companies Acts, 1862-1898, and among other objects for which the company was incorporated were—to acquire copper mines in any part of

1



liability can arise. I agree with Kennedy J., who has pointed out in his judgment that, though there are general provisions as to the company carrying on business in foreign countries, there is always the underlying and essential fact of its incorporation as an English company and the fundamental fact that it is a limited company. Prima facie the provisions of the memorandum of association must be taken to give power to do things not inconsistent with the constitution of the company under the memorandum and articles of association, but it cannot be assumed that because there is liberty to trade in a foreign country, the company is released from the fundamental condition which limits the liability of its members. To arrive at any other conclusion there must be something more than the fact that the company, which is a limited company, is authorized by its memorandum of association to do certain things. The authority to do these things is given to a limited company, and it can only do them subject to the limited liability of its shareholders, which is a fundamental condition of its existence. Certain authorities have been cited to us, of which certainly the English authorities appear to be entirely consistent with the view that I have expressed. In each of the two cases *Bank of Australasia v. Harding* (1) and *Bank of Australasia v. Nias* (2) the defendant, who was held liable by foreign law, he himself not being resident on the spot, and not being served with process according to English law, was a member of a company whose constitution provided for the very thing that was done. Being a member of a company so constituted, of course he could not avoid being responsible, and he was held to be made liable in terms to which he had expressly consented. In *Copin v. Adamson* (3) an effort was made in the second replication in an action on a foreign judgment to fix the shareholder in a French (4) company with liability, under the law of France, the country where the work of the company had been carried on, without reference to the statutes and articles of association of the company, and this attempt failed, for the Court held that his rights must be ascertained with reference to the contract to which he himself was a party. It was also said that there were decisions in the Courts of the United States which supported the arguments put forward on behalf of the plaintiffs, and the case relied on was *Pinney v. Nelson* (5). When that case is examined it appears to be distinguishable from the present one upon the grounds stated by Kennedy J. in his judgment. By the constitution of the company in that case there were provisions out of which the Court inferred that there was an express agreement, to which all the shareholders must be taken to be parties, that

(1) 9 C. B. 661.

(2) 16 Q. B. 717.

(3) L. R. 9 Ex. 345.

(4) The name of the company is given in the report as "*Societe de Commerce de France, Limited*," but see Lord Cairns's judgment in *C. A.*, 1 Ex. D. at p. 18; the appeal was on the first replication alone, which did rely on the statutes of the company.—F. P.

(5) 183 U. S. 144, 46 L. ed. 125.

the business of the company should be conducted in a foreign State. The inference of fact was that the company could be said to be a party to the initiation of the company must be taken to have authorized the company in California, that being the special object of the company was incorporated. That was the inference. It is not for us to canvass whether it was the case in that case. In the case before us there is no material on which the inference was drawn. It is to me that the case is distinguishable from the opinion the decision of the learned judge must be dismissed.¹⁸

WHITMAN v. OXFORD NATIONAL BANK

1899. 176 U. S. 559, 44 L. ed. 587.

THIS was an action brought in the Circuit Court of the States for the Southern District of New York against the Bank of Oxford, a national banking association established under the laws of the United States, doing business at Oxford in the State of Pennsylvania. Whitman, a citizen of the State of New York, brought the action under the provisions of the constitution of the State of Kansas, for a debt of more than \$2000 due to the Arkansas City Investment Company, a corporation of the State of Kansas, in which the defendant was a stockholder.

The constitution of the State of Kansas provides in article 12, section 2, as follows:

"Dues from corporations shall be secured from the stockholders to an additional amount equal to the amount owned by each stockholder; and such other provisions shall be provided by law; but such individual liabilities shall not be a lien on the road corporations, nor corporations for other purposes."

The General Statutes of 1868 of that State contain the following provisions:

"Sec. 32. If any execution shall have been issued against the property or effects of a corporation, except a corporation or charitable corporation, and there cannot be found whereon to levy such execution, then the same may be levied against any of the stockholders, to an extent equal to the amount owned by such stockholder."

¹⁸ See *Leyner Engineering Works v. Kepner* (1909) 170 Fed. 362; *Chesley v. Matthiesen* (1909) 170 Fed. 362; *Chesley v. Matthiesen* 19 N. Dak. 18, 121 N. W., 73; 6 Col. Law Rev. 4, 1909, 9 Col. Law Rev. 285, 492; and 10 Col. Law Rev. 285, 492.

¹⁹ Small portion of statement and opinion omitted.

amount of stock by him or her owned, together with any amount unpaid thereon; but no execution shall issue against any stockholder, except upon an order of the court in which the action, suit or other proceeding shall have been brought or instituted, made upon motion in open court, after reasonable notice in writing to the person or persons sought to be charged; and, upon such motion, such court may order execution to issue accordingly; or the plaintiff in the execution may proceed by action to charge the stockholders with the amount of his judgment."

"Sec. 40 (as amended in 1883). Laws 1883, c. 46, p. 88. A corporation is dissolved—first, by the expiration of the time limited in its charter; second, by a judgment of dissolution rendered by a court of competent jurisdiction; but any such corporation shall be deemed to be dissolved for the purpose of enabling any creditors of such corporation to prosecute suits against the stockholders thereof to enforce their individual liability, if it be shown that such corporation has suspended business for more than one year, or that any corporation now so suspended from business shall for three months after the passage of this act fail to resume its usual and ordinary business."

"Sec. 44. If any corporation, created under this or any general statute of this State, except railway or charitable or religious corporations, be dissolved, leaving debts unpaid, suits may be brought against any person or persons who were stockholders at the time of such dissolution, without joining the corporation in such suit; and if judgment be rendered, and execution satisfied, the defendant or defendants may sue all who were stockholders at the time of dissolution, for the recovery of the portion of such debt for which they were liable, and the execution upon the judgment shall direct the collection to be made from property of each stockholder, respectively; and if any number of stockholders (defendants in the case) shall not have property enough to satisfy his or their portion of the execution, then the amount of deficiency shall be divided equally among all the remaining stockholders, and collections made accordingly, deducting from the amount a sum in proportion to the amount of stock owned by the plaintiff at the time the company dissolved." * * *

The defendant moved the Circuit Court of the United States to direct a verdict in his favor, upon the ground that it had no jurisdiction to enforce a statutory remedy of the State of Kansas. The court denied the motion, directed a verdict for the plaintiff, overruled a motion for a new trial, and entered a final judgment for the plaintiff. 76 Fed. Rep. 697. That judgment was affirmed by the Circuit Court of Appeals. 51 U. S. App. 536. The defendant thereupon applied for and obtained this writ of certiorari. 168 U. S. 710.

MR. JUSTICE BREWER, after stating the case, delivered the opinion of the court.

By section 1 of article 12 of the constitution definite liability is cast upon each stockholder of religious and charitable corporations. This liability is to the extent of the amount equal to the value of the stock owned by him. The word "liability" is one of general import, and includes all contractual obligations. Whether broad liabilities for torts, either before or after judgment, or upon it we express no opinion. "Liabilities," are not merely directory to the legislature for such liability, but of themselves define the constitution is self-executing. Willis v. State, 140. The discretion of the legislature extended by the clause "and such other means as may be provided by law." A failure of the legislature to create modes of procedure may, it is true, make the provision inoperative, but does not destroy the liability. This is the obvious meaning of the constitutional provision, but does not destroy the liability by the act of the legislature prescribing the mode of procedure. This is the obvious meaning of the constitutional provision. This is the simplest and most obvious interpretation of the provision. This is the most sensible, is the most likely to be that of its adoption." Lamar, Justice, in Lake County v. Lake, 662, 671.

But this constitutional provision does not prevent the legislature of Kansas from acting on the subject. The constitution and the statutes are to be taken together. The constitution is a part of the law; and it serves no good purpose to say that the legislature has no remedy. Remedies a creditor of a corporation might have, would rest upon a stockholder if either considered alone and unaided by the other.

In section 32 of chapter 23 of the General Statutes, passed before the organization of the corporation, the legislature prescribed the mode of enforcing liability, and if such were needed declared to be enforced. It may be either by motion in a court, or by a direct action by the corporation. It has been rendered against the corporation and turned unsatisfied, or by a direct action by the corporation. Neither remedy can be made effective against a stockholder unless by due diligence. It may be brought within the jurisdiction of such court. See *Howell v. Mangelsdorf*, 144 U. S. 41.

Whatever else may be said about the remedy, it is available to every creditor of a corporation. The adjustment between the claims of the stockholders and the adjustment between the claims of the individual shares of the corporate obligation is a tendency to carry on business through the corporation and the freedom from personal liability. Corporate action, it cannot be said that this is open to judicial condemnation.

The liability which by the constitution and statutes is thus declared to rest upon the stockholder, though statutory in its origin, is contractual in its nature. It would not be doubted that if the stockholders in this corporation had formed a partnership, the obligations of each partner to the others and to creditors would be contractual, and determined by the general common law in respect to partnerships. If Kansas had provided for partnerships, with limited liability, and these parties, complying with the provisions of the statute, had formed such a partnership, it would also be true that their obligations to one another and to creditors would be contractual, although only in the statute was to be found the authority for the creation of such obligations. And it is none the less so when these same stockholders organized a corporation under a law of Kansas, which prescribed the nature of the obligations which each thereby assumed to the others and to the creditors. While the statute of Kansas permitted the forming of the corporation under certain conditions, the action of these parties was purely voluntary. In other words, they entered into a contract authorized by statute.

Flash v. Conn, 109 U. S. 371, is much in point. In that case a corporation was organized in the State of New York, under an act of legislature, which contained this provision:

"Sec. 10. All the stockholders of every company incorporated under this act shall be severally individually liable to the creditors of the company in which they are stockholders, to an amount equal to the amount of stock held by them respectively, for all debts and contracts made by such company, until the whole amount of capital stock fixed and limited by such company shall have been paid in, and a certificate thereof shall have been made and recorded as prescribed in the following section."

An action was brought in Florida against one of the stockholders, and on error to this court it was held that the stockholder was liable, the court saying (p. 377):

"We think the liability imposed by section 10 is a liability arising upon contract. The stockholders of the company are by that section made severally and individually liable, within certain limits, to the creditors of the company for its debts and contracts. Every one who becomes a member of the company by subscribing to its stock assumes this liability, which continues until the capital stock is all paid up and a certificate of that fact is made, published and recorded."

And again, after noticing the rulings of the Court of Appeals of the State of New York (p. 379):

"If this were a case arising in the State of New York we should therefore follow the construction put upon the statute by the courts of that State. The circumstance that the case comes here from the State of Florida should not leave the statute open to a different construction. It would be an anomaly for this court to put one interpretation on the statute in a case arising in New York, and a

different interpretation in a case arising from this action, therefore, is that this action was not brought in the nature of a penalty.

"The right of the plaintiffs to sue upon having jurisdiction of the subject-matter before the court is clear. *Dennick v. Railroad Co.*, 103

And finally, in reference to the objection at law against a single stockholder instead of the corporation (p. 380):

"But in this case the statute makes every stockholder liable for the debts of the company for the amount of his stock. This liability is fixed on the liability of other stockholders. In bringing in other stockholders or creditors recovered judgment against the company, the corporation thereon, which has been returned by the stockholder, and no other creditor can. Such action without objection in the courts of New York is authorized by the statute relied on in this case. *Shilling v. Railroad Co.*, 371; *Weeks v. Suydam*, 64 N. Y. 173; *Hart v. Railroad Co.*, 334; *Rocky Mountain Nat. Bank v. Bliss*,

In *Richmond v. Irons*, 121 U. S. 27, it was presented whether the individual liability of a stockholder in a national bank survived as against his admission to the corporation (p. 55):

"Under that act the individual liability is an essential element in the contract by which the stockholder becomes a member of the corporation. It is voluntary subscription for and accepting shares of stock as a part of every contract, debt and engagement entered into much so as if they were made directly by the stockholder or by the corporation. There is nothing to prevent that the obligation arising under these contracts should not have the same force and effect, in all respects, as any other contracts of the individual."

In *Concord First National Bank v. Hawley*, in which one national bank was sought to be established in another national bank, was this declared:

"In the present case it is sought to escape the liability of a national bank to respond to an assessment by the stockholder not contractual, but statutory."

"Undoubtedly, the obligation is declared to be the ownership of the stock, and in that case it is statutory. But as the ownership of the stock is from the voluntary act of the stockholder, having agreed or contracted to be subject to the assessment,"

Similar are the views entertained by the

sas. (After referring to several authorities, the learned Justice proceeded:)

And as this liability is one which is contractual in its nature, it is also clear that an action therefor can be maintained in any court of competent jurisdiction. *Dennick v. Railroad Company*, 103 U. S. 11; *Huntington v. Attrill*, 146 U. S. 657.

Similar views have been expressed by the highest courts of several States in like actions based upon the same Kansas constitutional and statutory provisions. *Ferguson v. Sherman*, 116 California, 169; *Bell v. Farwell*, 176 Illinois, 489; *Hancock National Bank v. Ellis*, 172 Mass. 39; *Western National Bank v. Lawrence*, 117 Michigan, 669; *Guerney v. Moore*, 131 Missouri, 650. See also *Paine v. Stewart*, 33 Connecticut, 516; *Cushing v. Perot*, 175 Penn. St. 66; *Rhodes v. United States National Bank*, (U. S. Ct. Ap. 7th Cir.) 24 U. S. App. 607; *Bank of North America v. Rindge*, (U. S. Cir. Ct. S. Dist. Cal.) 57 Fed. Rep. 279; *McVickar v. Jones*, (Cir. Ct. Dist. N. H.) 70 Fed. Rep. 754; *Mechanics' Savings Bank v. Fidelity Insurance Company*, (Cir. Ct. E. Dist. Penn.) 87 Fed. Rep. 113; *Dexter v. Edmands*, (Cir. Ct. Mass.) 89 Fed. Rep. 467; *Brown v. Trail*, (Cir. Ct. Dist. Md.) 89 Fed. Rep. 641.

We see no error in the judgment of the Circuit Court of Appeals, and it is, therefore,

Affirmed.

MR. JUSTICE PECKHAM dissented.

KNICKERBOCKER TRUST COMPANY v. ISELIN.

1906. 185 N. Y. 54, 77 N. E. 877.

APPEAL, by permission, from an order of the Appellate Division of the Supreme Court in the first judicial department, entered December 23, 1905, which affirmed an interlocutory judgment of Special Term overruling a demurrer to the complaint.

The following question was certified: "Does the complaint state facts sufficient to constitute a cause of action?" The nature of the action and the facts, so far as material, are stated in the opinion.

O'BRIEN, J.—The questions in this case arise upon a demurrer to the complaint on the ground that it does not state a cause of action. The purpose of the action was to enforce a statutory liability of the defendant as a stockholder in a Maryland corporation for a debt due to the plaintiff.

The action was commenced on the 19th of November, 1904, and the complaint alleges in substance the following facts: That the plaintiff is a domestic corporation; that the City Trust and Banking Company was a Maryland corporation; that each stockholder therein is liable under the laws of that state to creditors of the corporation

RELATION BETWEEN CREDITOR

for double the amount of stock at the p corporation; that the plaintiff loaned to on April 20, 1903, the sum of \$100,000 defendant was then a stockholder in 100 shares of its stock at the par value corporation was then insolvent, and on placed in the hands of a receiver; tha plaintiff on said loan the sum of \$49,1 manded against the defendant for \$2,0

The question is whether upon these f tained in the courts of this state, it bein gle creditor against a single stockholde Sherman (148 N. Y. 9) is to the effect be maintained, and that case seems to the more recent decisions of the Sup States. If I understand these decision ity of stockholders in such cases is no liability to be enforced primarily at the poration and in the state creating the Rankin, 197 U. S. 154; Middletown N M. R. Co., Id. 394; Hale v. Allinson, there ever was any doubt as to the true was decided in the Marshall case, it has tion that has been enacted both in thi the decision, and which was in force menced.

By chapter 337 of the Laws of Maryl provided as follows: "The exclusive 1 against stockholders of all rights existi lic General Laws * * * shall be, siding in the State of Maryland, by bill creditor's bill filed against such stockho itors on behalf of themselves and all otl tion who may come in and make themse chapter 101 of the laws of that state was further enacted: "The stockholder shall be held individually responsible e one for another for all contracts, debts such corporation to the extent of the ar at the par value thereof in addition to 1 stock. * * * And the liability of si asset of the corporation for the benefit itors of any such corporation, if necessa corporation, and shall be enforceable o ings by a receiver, assignee or trustee under the orders of a court of competen

It was held that these statutes affecte plied to actions pending when the sar

Bank v. Snyder, 100 Md. 57; Murphy v. Wheatley, Id. 358.) So that when this action was commenced it would not lie at the home of the insolvent corporation in its present form.

The law of New York on this subject is now to be found in § 54 of the Stock Corporation Law (L. 1890, ch. 564, § 57, as amd. L. 1892, ch. 688 and L. 1901, ch. 354) as follows: "Every holder of capital stock not fully paid, in any stock corporation, shall be personally liable to its creditors, to an amount equal to the amount unpaid on the stock held by him for debts of the corporation contracted while such stock was held by him. As to existing corporations the liability imposed by this section shall be in lieu of the liability imposed upon stockholders of any existing corporation, under any general or special law, (excepting laws relating to moneyed corporations, and corporations and associations for banking purposes), on account of any indebtedness hereafter contracted or any stock hereafter issued; but nothing in this section contained shall create or increase any liability of stockholders of any existing corporation under any general or special law. The stockholders of every stock corporation shall jointly and severally be personally liable for all debts due and owing to any of its laborers. * * *"

When the case of *Marshall v. Sherman* is read in the light of these statutes it would seem to be clear that this action was not, when commenced, maintainable either under the laws of New York or Maryland. In New York all liability for paid-up stock seems to have been swept away, whatever the form of the action, except as to moneyed corporations, and debts due to laborers, etc. In Maryland the liability is still retained, but must be asserted in a particular form of action.

It is argued, however, that the demurrer admits the foreign law as stated in the complaint, though clearly stated erroneously. The statement in the complaint is in this respect quite ambiguous. It is stated that "by virtue * * * of the aforesaid laws of Maryland as defined, construed, administered and enforced by the courts of that State defendant is personally and individually indebted to the plaintiff to an amount equal to double the amount of stock at par," etc. It may be and probably is true that he is personally and individually liable, but it is not true that he is liable in the present form of action, and the complaint does not specifically or plainly allege that he is, and the demurrer does not admit any facts not well pleaded. But I think there is a more conclusive answer to this point. When a pleading contains allegations of foreign law they are not admitted by a demurrer. (*Finney v. Guy*, 189 U. S. 335.) This is but a corollary of another proposition which is equally well settled. Proof of foreign law by experts, though ever so clear and though uncontradicted, is not conclusive, since the court must examine and determine the law for itself, and a demurrer has no greater effect than uncontradicted proof. (*Laing v. Rigney*, 160 U. S. 531.) It is true that foreign law is ordinarily proved as a fact, still

it is not in its essential nature a fact any more than it is a fact.

What has been said is a sufficient answer to the contention that the case of *Howarth v. Angle* is conclusive in its favor. That case does not depend on the law of the two states as this case does. That case was of an insolvent bank of the state of Washington, and the defendant on account of his ownership of an equal and ratable proportion of a deficiency of the capital stock of said bank. As a result of the Washington courts the receiver had no action and the amount of the deficiency had been obtained both by the courts of that state and by the defendant's promise valid at common law, because the defendant took stock in the Tacoma Bank in violation of the law, which he impliedly agreed to bear the consequences of, and thus become a stockholder. (*Lowry v. Tacoma Bank*). That burden is an asset vested in the receiver of this state the same as a promissory note, which is valid in Washington are in force here, but because the defendant assented to the conditions upon which the liability was created. * * * While the liability is, for convenience, statutory, because the statute, which is the basis of the liability, affixed the obligation to the ownership of stock, the liability is contractual and springs from an implied promise, a substantial difference between the liability for stock subscription, which is an express contract to pay for it (*Stoddard v. Lum*, 159 N. Y. 20), and the unpaid deficiency of assets assumed by a member of the corporation through the stock subscription, which a contract is implied to perform the conditions upon which stock may be owned. (*Richmond v. American Bank*). * * * The express promise runs to the benefit of the creditors enforced by it, while the implied promise runs to the benefit of the state, may, according to the common law of the state, be enforced for the benefit of creditors by a receiver appointed to wind up its affairs."

The order appealed from should be reversed, and the demurrer sustained, with costs to be paid over on payment of costs.

Question certified answered in the negative.
VANN, WERNER, WILLARD BARTLETT and
CULLEN, Ch. J., and HAIGHT, J., concur in
*Ordered accordingly.*²⁰

²⁰ See *Marsh v. Kaye* (1901) 168 N. Y., 196, 61 N. E. 1104; *Edwards v. Wells* (1911) 200 N. Y., 472, 93 N. E. 1104.—Eds

Section 4.—Who is Liable as Stockholder? Effect of Transfer of Shares.

OHIO VALLEY NATIONAL BANK v. HULITT.

1906. 204 U. S. 162, 51 L. ed. 423, 27 Sup. Ct. 179.

THIS case was begun in the United States Circuit Court by John Hulitt as receiver of the First National Bank of Hillsboro, Ohio, against the Ohio Valley National Bank, to recover the amount of an assessment upon certain shares of the stock of the Hillsboro Bank, which had become insolvent, which assessment was directed by the Comptroller of the Currency in accordance with the provisions of the National Bank Act. The case was tried upon an agreed statement of facts, from which it appears that on March 18, 1893, one Overton S. Price, for a loan of \$10,000, gave his promissory note of that date to the Ohio Valley Bank, due ninety days after date, payable to his own order and indorsed by him, and deposited as collateral security for the note, among other securities, fifty shares of stock of the said First National Bank of Hillsboro, Ohio. The note had a power of sale attached to it, signed by Price, and authorizing the holder to sell or collect any portion of the collateral, at public or private sale, on the non-performance of the promise, and at any time thereafter without advertising or otherwise giving Price notice, and providing that in case of public sale the holder might purchase without liability to account for more than the net proceeds of the sale.

On December 25, 1893, Price died, leaving the note due and unpaid, and no payments have been made thereon except as hereinafter stated.

On June 18, 1894, the bank made a transfer of the pledged stock of the First National Bank of Hillsboro, and also of certain other stock in the Dominion National Bank of Bristol, Va., to one Henry Otjen, an employe of the bank, and pecuniarily irresponsible. The shares were transferred on the books of the banks and new certificates issued in the name of Otjen and delivered to him on July 7, 1894. Otjen indorsed the certificates in blank. No money passed in consideration of the transfer, and none was expected, nor was any credit given or indorsed on the note by reason thereof.

The transfer was made upon the understanding and agreement between Otjen and the bank that Otjen should hold the stock as security for the indebtedness of the estate of Price upon the note, he to apply any amounts which he might realize from said stock as credits upon the note. In pursuance of this agreement Otjen subsequently paid the bank sums received from the Dominion National Bank on account of dividends received until the sale of that stock, when the proceeds of sale were likewise applied by him upon the note.

On February 19, 1896, the bank prepared the estate of Price, and at that time believed to Otjen to afford a reasonable security for of \$4,484, indorsed a credit for that sum to "Forty-four hundred and eighty-four (\$4, of within note June 18, '94, being proceeds Dominion National Bank and 20 shares of of Hillsboro, O." The bank filed its proof of the indebtedness upon the note; that not for said credit, and the same was not entered that all dividends arising upon the distribution were applied upon the note.

The Hillsboro bank continued to do business. From the date of transfer at all times the books of the Hillsboro bank in the name of ing on the books to connect the Ohio Valley the stock, or to indicate that it had any defendant bank at no time performed any exercised or attempted to exercise any of the in said bank, or of the Dominion National stated were in legal intendment of that Charlesley National Bank procured the shares to because it was unwilling to assume the responsibility of a stockholder in respect thereto. The appeals held the bank liable as a stockholder, directed judgment accordingly.

MR. JUSTICE DAY after making the foregoing the opinion of the court.

Section 5151 of the Revised Statutes requires holders of every national banking association to be equally responsible, equally and ratably, not only for contracts, debts and engagements of such association of the amount of their stock therein, but in addition to the amount invested in such stock undertakes to hold all shareholders responsible for losses arisen under varying circumstances as to each shareholder.

In *Anderson v. Philadelphia Warehouse* it was held that the mere pledgee who had transferred on the books of the bank and an irresponsible person, in that instance a shareholder of the company, and this although the transfer was for the purpose of avoiding liability which the shareholders of the bank, in case of insolvency, the opinion, Mr. Chief Justice Waite, speaking for the court, held that the real owner might be held lia

in that case the facts showed the warehouse company, sought to be held as a shareholder, was never other than a pledgee, and that notwithstanding the transfer to the irresponsible person, the real ownership of the stock remained in the original holder.

In *Pauly v. The State Loan & Trust Company*, 165 U. S. 606, the subject was considered at length, and it was held that one who was described in the certificate as a pledgee, and who in good faith held the shares as such, was not a shareholder subject to the personal liability imposed by section 5151. The previous cases in this court were reviewed, and, in summing up the rules relating to the liability of shareholders in national banks, deducible from previous decisions, among other things it was said: "That the real owner of the shares of the capital stock of a national banking association may, in every case, be treated as a shareholder within the meaning of section 5151." And again: "The object of the statute is not to be defeated by the mere forms of transactions between shareholders and their creditors. The courts will look at the relations of parties as they actually are, or, as, by reason of their conduct, they must be assumed to be for the protection of creditors. Congress did not say that those only should be regarded as shareholders, liable for the contracts, debts and engagements of the banking association, whose names appear on the stock list distinctly as shareholders. A mistake or error in keeping the official list of shareholders would not prevent creditors from holding liable all who were, in fact, the real owners of the stock, and as such had invested money in the shares of the association. As already indicated, those may be treated as shareholders, within the meaning of section 5151, who are the real owners of the stock, or who hold themselves out, or allow themselves to be held out, as owners in such way and under such circumstances as, upon principles of fair dealing, will estop them, as against creditors, from claiming that they were not, in fact, owners."

And in *Rankin v. Fidelity Trust Company*, 189 U. S. 242, 252, the doctrine was stated that a defendant who was in fact the owner of shares of stock could not avoid liability by listing them in the name of another, notwithstanding it might do so if it were the mere pledgee of the stock; and further, that the case then under consideration turned upon the actual ownership of the shares, which question was properly left to the jury. And to the same effect are well considered cases in other courts, Federal and state. It was held that the real owner might be charged, although his name never appeared upon the books of the bank. *Davis v. Stevens*, 17 Blatch. 259, 7 Fed. Cas. 3653, opinion by Mr. Chief Justice Waite; *Houghton v. Hubbell*, Circuit Court of Appeals, First Circuit, 91 Fed. Rep. 453; *Laing v. Burley*, 101 Illinois, 591; *Lesassier v. Kennedy*, 36 La. Ann. 539.

Assuming then the established doctrine to be that the mere pledgee of national bank stock cannot be held liable as a shareholder so

long as the shares are not registered in the responsible person has been selected as the person to whom it is equally settled, both from the time the liability and the decisions which have been made by the real owner of the shares may be held responsible for the shares are not registered in his name. The law looks through subterfuges and appears to place the liability upon the shareholder to whom the shares are registered.

Applying these principles to the case at hand, there can be no doubt of the liability of the Ohio National Bank in this case. Conceding that it was exempt from the liability which it held to the stock was that of a pledgee and not as owner, what was the result of the death of Price and the credit of the note upon the note and its presentation for all the representatives of Price's estate? As the record shows, the stock was originally delivered to the bank by public or private sale for the liquidation of the estate of Price the bank caused the signature of Otjen. After proof of the claim against the Price estate were credited upon the note, the bank followed literally the authority of the power of attorney and sold the stock at public or private sale to the purchaser, we take it there could be no doubt that they thus have become the real owner of the stock. In the cases heretofore cited, the same principle applies to the terms of the statute. We think what was done here had the same effect; the bank applied to the court for the consent of the pledgor, and thus vested the title in the bank.

It is urged that although the indorsement was in the form in which it was presented to Price, the bank's credit as of June 18, 1894, being procured, there never was a sale in fact, and that the result is anything shown in the case from showing an actual transaction between the parties.

Conceding, for this purpose, that Price's estate insisted upon a strict performance of the duty of the authority given to the bank as to the disposition of the stock, if the representative of Price desired to prevent him from waiving a strict compliance with the law and permitting the bank to acquire title to the stock on the value on the note. This is in fact what was done. In selling the stock, the bank, in executing the power of attorney, indorsed what it deemed the value of the stock, upon the note, and reduced by the amount of the stock presented the note to the administrator. The bank allowed the claim in this form, as it is

subsequent dividends upon the claim were paid to the bank. By this transaction, who became the real owner of the stock? Certainly not Otjen, for it is not contended that he was other than a mere holder of the stock as collateral security to the bank without any beneficial interest. Price had died, and his representative had allowed the claim, showing the application of the value of the stock as a credit upon the note. If Price's representative could have objected to the form in which the bank liquidated the pledge, he did not do so, but accepted the bank's method of divesting him of title by allowing the claim with the credit upon it. The bank thus became the beneficial owner of the stock, and had the Hillsboro National Bank continued solvent it certainly could not have denied to the Ohio Valley Bank after this transaction the rights and privileges of a stockholder.

As we have seen, this court in construing the banking act has not limited the liability to the registered stockholders. (While the registered stockholders may be held liable to creditors regardless of the true ownership of the stock, and the pledgee of the stock not appearing otherwise, is not liable, although the registered stockholder may be an irresponsible person of his choice, yet where the real ownership of the stock is in one his liability may be established, notwithstanding the registered ownership is in the name of a person fictitious or otherwise, who holds for him.

We think the Circuit Court of Appeals did not err in holding the bank, in view of the facts shown in the case, as the true owner and responsible shareholder of the stock in question.

*Judgment affirmed.*¹

MCDONALD v. DEWEY.

1906. 202 U. S. 510, 50 L. ed. 1128, 26 Sup. Ct. 731.²

A bill in equity to enforce an assessment of \$86 a share on 105 shares of stock of the First National Bank of Orleans, Neb., which failed on May 20, 1897. These shares, having been originally owned by Charles P. Dewey, were sold by him in December, 1894, and in January, 1895. Eighty shares were duly transferred on the books of the bank within a few weeks after the sale. The remaining twenty-five shares had been previously transferred by Dewey to his agent, Frederick L. Jewett, who was admitted to be irresponsible, and stood on the books of the bank in the name of Jewett, when the bank went into the hands of a receiver, on May 20, 1897, although they had been sold by Dewey. * * *

¹ See *Henderson v. Mayfield Woolen Mills* (1907) 153 Ala. 625, 45 So. 211; *Brinkley v. Hambleton* (1887) 67 Md. 169, 8 Atl. 904; *South Milwaukee Co. v. Murphy* (1902) 112 Wis. 614, 88 N. W. 583, 58 L. R. A. 82.—Eds.

² Statement abridged. Portion of dissenting opinion of Mr. Justice White omitted.—Eds.

The Circuit Court found that the stock was transferred through Jewett, who acted merely as a broker, and had no interest in the stock, but held it for the bank. The bank failed about two years and five months after that the bank was insolvent in December 1892, at the time Dewey sold the hundred and twenty-five shares, who was vice-president of the bank and ought to have known, that fact; that the twenty-five shares, were not transferred and still stood in the name of Jewett; that the claims of the creditors of the bank at the time Dewey sold his stock and remained unsatisfied, aggregated \$11,839.15, of which, however, the bank was not liable, and that of this the ratable sum a decree was rendered.

On appeal by the receiver to the Circuit Court of the Circuit Court was reversed, and the decree to be entered for the full amount of the five shares standing in the name of Jewett, and that as to the eighty shares there could be no recovery, as the bank was insolvent at the time of the transfer, and the transfer was made with knowledge of evading liability; but that there was no proof of the additional fact that the bank was insolvent; that as to the twenty-five shares, as he had not surrendered the certificates, the officers such data as to enable them to transfer the shares. The case was remanded to the Circuit Court to render a decree against Dewey for the twenty-five shares. From this decree appeal. * * *

MR. JUSTICE BROWN delivered the opinion of the court.

Three sections of the National Bank Act, the margin,¹ are pertinent in connection with the case.

¹ Sec. 5139. The capital stock of each association shall be divided into shares of one hundred dollars each, and be transferable on the books of the association as provided in the by-laws or articles of association. The transfer of shares by such transfer shall, in proportion to the rights and liabilities of the prior holder, be made in the articles of association. The security of the existing creditors of the association shall be maintained.

(The shares of this Nebraska bank were transferred to the bank, in person or by attorney, on surrender of the shares proposed to be transferred.)

Sec. 5210. The president and cashier of each association shall cause to be kept at all times a full and correct list of the residences of all the shareholders in the association, and the office where its business is conducted, subject to the inspection of all the shareholders.

That the transfer of stock in corporations, even when in failing circumstances, should not be unduly impeded, is essential not only to the prosperity of such corporations and the value of their stock, but to the interest of stockholders who may desire for legitimate reasons to change their investments or to raise money for debts incurred outside the business of such corporation. *Bank v. Lanier*, 11 Wall. 369, 377. At the same time the frequency with which such transfers are made for the purpose of evading the double liability imposed by the National Banking Act, has given rise to a large amount of litigation turning upon their legality. In this connection certain propositions have been laid down by so many courts and in so many cases that they may be regarded as fundamental principles of law applicable to all cases of this character.

(1) That a party, who by way of pledge or collateral security for a loan of money, accepts stock of a national bank and puts his name on the registry as owner, incurs an immediate liability as a stockholder, and cannot relieve himself therefrom by making a colorable transfer of his stock to another person for his own benefit, as was done by the sale to Jewett in this case. *National Bank v. Case*, 99 U. S. 628; *Marcy v. Clark*, 17 Massachusetts, 329; *Nathan v. Whitlock*, 9 Paige, 152; *Cook on Stockholders*, § 263.

(2) The same result follows if the stockholder, knowing, or having good reason to know, the insolvency of the bank, colludes with an irresponsible person with design to substitute the latter in his place, and thus escape individual liability and transfers his stock to such person. It is immaterial in such case that he may be able to show a full or partial consideration for the transfer as between himself and the transferee. *Bowden v. Johnson*, 107 U. S. 251.

Upon the other hand, in *Whitney v. Butler*, 118 U. S. 655, certain stockholders employed an auctioneer to sell their shares at public auction. They were bidden in by a purchaser who paid the auctioneer for them and received from him the certificate of stock with a power of attorney to transfer the same in blank. The auctioneer paid the money to the original owner of stock, but no formal transfer was made on the books of the bank. Shortly afterward the bank became insolvent and went into the hands of a receiver, who made an assessment upon the original stockholders. We held that the responsibility of the stockholders ceased, upon the surrender of

tion, and the officers authorized to assess taxes under state authority, during business hours of each day in which business may be legally transacted. A copy of such list, on the first Monday of July of each year, verified by the oath of such president or cashier, shall be transmitted to the Comptroller of the Currency.

Sec. 5151. The shareholders of every national banking association shall be held individually responsible, equally and ratably, and not one for another, for all contracts, debts and engagements of such association, to the extent of the amount of their stock therein, at the par value thereof, in addition to the amount invested in such shares; . . .

the certificate to the bank and the delivery of a power of attorney to transfer the stock. The controlling considerations were the fact that the stockholders, in making the sale, believing the fact that they had done all that they could do to make a valid sale of the stock and to get it on the stock register.

Under the English law a shareholder is not an irresponsible party for a nominal consideration if the purpose of the transfer be to escape liability. It must be out and out, and not merely colorable. No trust attached. Under such circumstances the transfer is released from liability, both as to the original stockholder and as to the other shareholders. Cook on Stock, 2d ed., § 859.

The law is quite different in this country. The original stockholder cannot be held liable if the bank be practically insolvent at the time the transfer is made, and the condition was known or ought to have been known to the stockholder making the transfer. If the bank be able to pay its debts as they matured and the creditors having ample security in the assets, the stockholders have no special interest in knowing whether the bank be insolvent or not. Their only recourse to them would be in the event of the insolvency of the bank. The transfer is valid if the bank be insolvent, and such insolvency has been known, to him from his relation to the bank. The transfer is *prima facie* valid, and shifts the responsibility, which can be laid only in case of bad faith, or evident liability.

This bad faith may be shown by the fact that the transfer was known to him to be insolvent; but not otherwise. The transfer would be valid if made to a person of known solvency, since the creditors could not suffer by the transfer. The court, however, went further and held that the transfer is valid unless made to an irresponsible person, or a person whose financial condition was known to him.

There was no such limitation in the case of *State Loan & Trust Co. v. State Loan & Trust Co.*, 165 U. S. 298, 41 S. Ct. 511, 4 L. Ed. 2d 1011, 1012, 1013, 1014, 1015, 1016, 1017, 1018, 1019, 1020, 1021, 1022, 1023, 1024, 1025, 1026, 1027, 1028, 1029, 1030, 1031, 1032, 1033, 1034, 1035, 1036, 1037, 1038, 1039, 1040, 1041, 1042, 1043, 1044, 1045, 1046, 1047, 1048, 1049, 1050, 1051, 1052, 1053, 1054, 1055, 1056, 1057, 1058, 1059, 1060, 1061, 1062, 1063, 1064, 1065, 1066, 1067, 1068, 1069, 1070, 1071, 1072, 1073, 1074, 1075, 1076, 1077, 1078, 1079, 1080, 1081, 1082, 1083, 1084, 1085, 1086, 1087, 1088, 1089, 1090, 1091, 1092, 1093, 1094, 1095, 1096, 1097, 1098, 1099, 1100, 1101, 1102, 1103, 1104, 1105, 1106, 1107, 1108, 1109, 1110, 1111, 1112, 1113, 1114, 1115, 1116, 1117, 1118, 1119, 1120, 1121, 1122, 1123, 1124, 1125, 1126, 1127, 1128, 1129, 1130, 1131, 1132, 1133, 1134, 1135, 1136, 1137, 1138, 1139, 1140, 1141, 1142, 1143, 1144, 1145, 1146, 1147, 1148, 1149, 1150, 1151, 1152, 1153, 1154, 1155, 1156, 1157, 1158, 1159, 1160, 1161, 1162, 1163, 1164, 1165, 1166, 1167, 1168, 1169, 1170, 1171, 1172, 1173, 1174, 1175, 1176, 1177, 1178, 1179, 1180, 1181, 1182, 1183, 1184, 1185, 1186, 1187, 1188, 1189, 1190, 1191, 1192, 1193, 1194, 1195, 1196, 1197, 1198, 1199, 1200, 1201, 1202, 1203, 1204, 1205, 1206, 1207, 1208, 1209, 1210, 1211, 1212, 1213, 1214, 1215, 1216, 1217, 1218, 1219, 1220, 1221, 1222, 1223, 1224, 1225, 1226, 1227, 1228, 1229, 1230, 1231, 1232, 1233, 1234, 1235, 1236, 1237, 1238, 1239, 1240, 1241, 1242, 1243, 1244, 1245, 1246, 1247, 1248, 1249, 1250, 1251, 1252, 1253, 1254, 1255, 1256, 1257, 1258, 1259, 1260, 1261, 1262, 1263, 1264, 1265, 1266, 1267, 1268, 1269, 1270, 1271, 1272, 1273, 1274, 1275, 1276, 1277, 1278, 1279, 1280, 1281, 1282, 1283, 1284, 1285, 1286, 1287, 1288, 1289, 1290, 1291, 1292, 1293, 1294, 1295, 1296, 1297, 1298, 1299, 1300, 1301, 1302, 1303, 1304, 1305, 1306, 1307, 1308, 1309, 1310, 1311, 1312, 1313, 1314, 1315, 1316, 1317, 1318, 1319, 1320, 1321, 1322, 1323, 1324, 1325, 1326, 1327, 1328, 1329, 1330, 1331, 1332, 1333, 1334, 1335, 1336, 1337, 1338, 1339, 1340, 1341, 1342, 1343, 1344, 1345, 1346, 1347, 1348, 1349, 1350, 1351, 1352, 1353, 1354, 1355, 1356, 1357, 1358, 1359, 1360, 1361, 1362, 1363, 1364, 1365, 1366, 1367, 1368, 1369, 1370, 1371, 1372, 1373, 1374, 1375, 1376, 1377, 1378, 1379, 1380, 1381, 1382, 1383, 1384, 1385, 1386, 1387, 1388, 1389, 1390, 1391, 1392, 1393, 1394, 1395, 1396, 1397, 1398, 1399, 1400, 1401, 1402, 1403, 1404, 1405, 1406, 1407, 1408, 1409, 1410, 1411, 1412, 1413, 1414, 1415, 1416, 1417, 1418, 1419, 1420, 1421, 1422, 1423, 1424, 1425, 1426, 1427, 1428, 1429, 1430, 1431, 1432, 1433, 1434, 1435, 1436, 1437, 1438, 1439, 1440, 1441, 1442, 1443, 1444, 1445, 1446, 1447, 1448, 1449, 1450, 1451, 1452, 1453, 1454, 1455, 1456, 1457, 1458, 1459, 1460, 1461, 1462, 1463, 1464, 1465, 1466, 1467, 1468, 1469, 1470, 1471, 1472, 1473, 1474, 1475, 1476, 1477, 1478, 1479, 1480, 1481, 1482, 1483, 1484, 1485, 1486, 1487, 1488, 1489, 1490, 1491, 1492, 1493, 1494, 1495, 1496, 1497, 1498, 1499, 1500, 1501, 1502, 1503, 1504, 1505, 1506, 1507, 1508, 1509, 1510, 1511, 1512, 1513, 1514, 1515, 1516, 1517, 1518, 1519, 1520, 1521, 1522, 1523, 1524, 1525, 1526, 1527, 1528, 1529, 1530, 1531, 1532, 1533, 1534, 1535, 1536, 1537, 1538, 1539, 1540, 1541, 1542, 1543, 1544, 1545, 1546, 1547, 1548, 1549, 1550, 1551, 1552, 1553, 1554, 1555, 1556, 1557, 1558, 1559, 1560, 1561, 1562, 1563, 1564, 1565, 1566, 1567, 1568, 1569, 1570, 1571, 1572, 1573, 1574, 1575, 1576, 1577, 1578, 1579, 1580, 1581, 1582, 1583, 1584, 1585, 1586, 1587, 1588, 1589, 1590, 1591, 1592, 1593, 1594, 1595, 1596, 1597, 1598, 1599, 1600, 1601, 1602, 1603, 1604, 1605, 1606, 1607, 1608, 1609, 1610, 1611, 1612, 1613, 1614, 1615, 1616, 1617, 1618, 1619, 1620, 1621, 1622, 1623, 1624, 1625, 1626, 1627, 1628, 1629, 1630, 1631, 1632, 1633, 1634, 1635, 1636, 1637, 1638, 1639, 1640, 1641, 1642, 1643, 1644, 1645, 1646, 1647, 1648, 1649, 1650, 1651, 1652, 1653, 1654, 1655, 1656, 1657, 1658, 1659, 1660, 1661, 1662, 1663, 1664, 1665, 1666, 1667, 1668, 1669, 1670, 1671, 1672, 1673, 1674, 1675, 1676, 1677, 1678, 1679, 1680, 1681, 1682, 1683, 1684, 1685, 1686, 1687, 1688, 1689, 1690, 1691, 1692, 1693, 1694, 1695, 1696, 1697, 1698, 1699, 1700, 1701, 1702, 1703, 1704, 1705, 1706, 1707, 1708, 1709, 1710, 1711, 1712, 1713, 1714, 1715, 1716, 1717, 1718, 1719, 1720, 1721, 1722, 1723, 1724, 1725, 1726, 1727, 1728, 1729, 1730, 1731, 1732, 1733, 1734, 1735, 1736, 1737, 1738, 1739, 1740, 1741, 1742, 1743, 1744, 1745, 1746, 1747, 1748, 1749, 1750, 1751, 1752, 1753, 1754, 1755, 1756, 1757, 1758, 1759, 1760, 1761, 1762, 1763, 1764, 1765, 1766, 1767, 1768, 1769, 1770, 1771, 1772, 1773, 1774, 1775, 1776, 1777, 1778, 1779, 1780, 1781, 1782, 1783, 1784, 1785, 1786, 1787, 1788, 1789, 1790, 1791, 1792, 1793, 1794, 1795, 1796, 1797, 1798, 1799, 1800, 1801, 1802, 1803, 1804, 1805, 1806, 1807, 1808, 1809, 1810, 1811, 1812, 1813, 1814, 1815, 1816, 1817, 1818, 1819, 1820, 1821, 1822, 1823, 1824, 1825, 1826, 1827, 1828, 1829, 1830, 1831, 1832, 1833, 1834, 1835, 1836, 1837, 1838, 1839, 1840, 1841, 1842, 1843, 1844, 1845, 1846, 1847, 1848, 1849, 1850, 1851, 1852, 1853, 1854, 1855, 1856, 1857, 1858, 1859, 1860, 1861, 1862, 1863, 1864, 1865, 1866, 1867, 1868, 1869, 1870, 1871, 1872, 1873, 1874, 1875, 1876, 1877, 1878, 1879, 1880, 1881, 1882, 1883, 1884, 1885, 1886, 1887, 1888, 1889, 1890, 1891, 1892, 1893, 1894, 1895, 1896, 1897, 1898, 1899, 1900, 1901, 1902, 1903, 1904, 1905, 1906, 1907, 1908, 1909, 1910, 1911, 1912, 1913, 1914, 1915, 1916, 1917, 1918, 1919, 1920, 1921, 1922, 1923, 1924, 1925, 1926, 1927, 1928, 1929, 1930, 1931, 1932, 1933, 1934, 1935, 1936, 1937, 1938, 1939, 1940, 1941, 1942, 1943, 1944, 1945, 1946, 1947, 1948, 1949, 1950, 1951, 1952, 1953, 1954, 1955, 1956, 1957, 1958, 1959, 1960, 1961, 1962, 1963, 1964, 1965, 1966, 1967, 1968, 1969, 1970, 1971, 1972, 1973, 1974, 1975, 1976, 1977, 1978, 1979, 1980, 1981, 1982, 1983, 1984, 1985, 1986, 1987, 1988, 1989, 1990, 1991, 1992, 1993, 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003, 2004, 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018, 2019, 2020, 2021, 2022, 2023, 2024, 2025, 2026, 2027, 2028, 2029, 2030, 2031, 2032, 2033, 2034, 2035, 2036, 2037, 2038, 2039, 2040, 2041, 2042, 2043, 2044, 2045, 2046, 2047, 2048, 2049, 2050, 2051, 2052, 2053, 2054, 2055, 2056, 2057, 2058, 2059, 2060, 2061, 2062, 2063, 2064, 2065, 2066, 2067, 2068, 2069, 2070, 2071, 2072, 2073, 2074, 2075, 2076, 2077, 2078, 2079, 2080, 2081, 2082, 2083, 2084, 2085, 2086, 2087, 2088, 2089, 2090, 2091, 2092, 2093, 2094, 2095, 2096, 2097, 2098, 2099, 2100, 2101, 2102, 2103, 2104, 2105, 2106, 2107, 2108, 2109, 2110, 2111, 2112, 2113, 2114, 2115, 2116, 2117, 2118, 2119, 2120, 2121, 2122, 2123, 2124, 2125, 2126, 2127, 2128, 2129, 2130, 2131, 2132, 2133, 2134, 2135, 2136, 2137, 2138, 2139, 2140, 2141, 2142, 2143, 2144, 2145, 2146, 2147, 2148, 2149, 2150, 2151, 2152, 2153, 2154, 2155, 2156, 2157, 2158, 2159, 2160, 2161, 2162, 2163, 2164, 2165, 2166, 2167, 2168, 2169, 2170, 2171, 2172, 2173, 2174, 2175, 2176, 2177, 2178, 2179, 2180, 2181, 2182, 2183, 2184, 2185, 2186, 2187, 2188, 2189, 2190, 2191, 2192, 2193, 2194, 2195, 2196, 2197, 2198, 2199, 2200, 2201, 2202, 2203, 2204, 2205, 2206, 2207, 2208, 2209, 2210, 2211, 2212, 2213, 2214, 2215, 2216, 2217, 2218, 2219, 2220, 2221, 2222, 2223, 2224, 2225, 2226, 2227, 2228, 2229, 2230, 2231, 2232, 2233, 2234, 2235, 2236, 2237, 2238, 2239, 2240, 2241, 2242, 2243, 2244, 2245, 2246, 2247, 2248, 2249, 2250, 2251, 2252, 2253, 2254, 2255, 2256, 2257, 2258, 2259, 2260, 2261, 2262, 2263, 2264, 2265, 2266, 2267, 2268, 2269, 2270, 2271, 2272, 2273, 2274, 2275, 2276, 2277, 2278, 2279, 2280, 2281, 2282, 2283, 2284, 2285, 2286, 2287, 2288, 2289, 2290, 2291, 2292, 2293, 2294, 2295, 2296, 2297, 2298, 2299, 2300, 2301, 2302, 2303, 2304, 2305, 2306, 2307, 2308, 2309, 2310, 2311, 2312, 2313, 2314, 2315, 2316, 2317, 2318, 2319, 2320, 2321, 2322, 2323, 2324, 2325, 2326, 2327, 2328, 2329, 2330, 2331, 2332, 2333, 2334, 2335, 2336, 2337, 2338, 2339, 2340, 2341, 2342, 2343, 2344, 2345, 2346, 2347, 2348, 2349, 2350, 2351, 2352, 2353, 2354, 2355, 2356, 2357, 2358, 2359, 2360, 2361, 2362, 2363, 2364, 2365, 2366, 2367, 2368, 2369, 2370, 2371, 2372, 2373, 2374, 2375, 2376, 2377, 2378, 2379, 2380, 2381, 2382, 2383, 2384, 2385, 2386, 2387, 2388, 2389, 2390, 2391, 2392, 2393, 2394, 2395, 2396, 2397, 2398, 2399, 2400, 2401, 2402, 2403, 2404, 2405, 2406, 2407, 2408, 2409, 2410, 2411, 2412, 2413, 2414, 2415, 2416, 2417, 2418, 2419, 2420, 2421, 2422, 2423, 2424, 2425, 2426, 2427, 2428, 2429, 2430, 2431, 2432, 2433, 2434, 2435, 2436, 2437, 2438, 2439, 2440, 2441, 2442, 2443, 2444, 2445, 2446, 2447, 2448, 2449, 2450, 2451, 2452, 2453, 2454, 2455, 2456, 2457, 2458, 2459, 2460, 2461, 2462, 2463, 2464, 2465, 2466, 2467, 2468, 2469, 2470, 2471, 2472, 2473, 2474, 2475, 2476, 2477, 2478, 2479, 2480, 2481, 2482, 2483, 2484, 2485, 2486, 2487, 2488, 2489, 2490, 2491, 2492, 2493, 2494, 2495, 2496, 2497, 2498, 2499, 2500, 2501, 2502, 2503, 2504, 2505, 2506, 2507, 2508, 2509, 2510, 2511, 2512, 2513, 2514, 2515, 2516, 2517, 2518, 2519, 2520, 2521, 2522, 2523, 2524, 2525, 2526, 2527, 2528, 2529, 2530, 2531, 2532, 2533, 2534, 2535, 2536, 2537, 2538, 2539, 2540, 2541, 2542, 2543, 2544, 2545, 2546, 2547, 2548, 2549, 2550, 2551, 2552, 2553, 2554, 2555, 2556, 2557, 2558, 2559, 2560, 2561, 2562, 2563, 2564, 2565, 2566, 2567, 2568, 2569, 2570, 2571, 2572, 2573, 2574, 2575, 2576, 2577, 2578, 2579, 2580, 2581, 2582, 2583, 2584, 2585, 2586, 2587, 2588, 2589, 2590, 2591, 2592, 2593, 2594, 2595, 2596, 2597, 2598, 2599, 2600, 2601, 2602, 2603, 2604, 2605, 2606, 2607, 2608, 2609, 2610, 2611, 2612, 2613, 2614, 2615, 2616, 2617, 2618, 2619, 2620, 2621, 2622, 2623, 2624, 2625, 2626, 2627, 2628, 2629, 2630, 2631, 2632, 2633, 2634, 2635, 2636, 2637, 2638, 2639, 2640, 2641, 2642, 2643, 2644, 2645, 2646, 2647, 2648, 2649, 2650, 2651, 2652, 2653, 2654, 2655, 2656, 2657, 2658, 2659, 2660, 2661, 2662, 2663, 2664, 2665, 2666, 2667, 2668, 2669, 2670, 2671, 2672, 2673, 2674, 2675, 2676, 2677, 2678, 2679, 2680, 2681, 2682, 2683, 2684, 2685, 2686, 2687, 2688, 2689, 2690, 2691, 2692, 2693, 2694, 2695, 2696, 2697, 2698, 2699, 2700, 2701, 2702, 2703, 2704, 2705, 2706, 2707, 2708, 2709, 2710, 2711, 2712, 2713, 2714, 2715, 2716, 2717, 2718, 2719, 2720, 2721, 2722, 2723, 2724, 2725, 2726, 2727, 2728, 2729, 2730, 2731, 2732, 2733, 2734, 2735, 2736, 2737, 2738, 2739, 2740, 2741, 2742, 2743, 2744, 2745, 2746, 2747, 2748, 2749, 2750, 2751, 2752, 2753, 2754, 2755, 2756, 2757, 2758, 2759, 2760, 2761, 2762, 2763, 2764, 2765, 2766, 2767, 2768, 2769, 2770, 2771, 2772, 2773, 2774, 2775, 2776, 2777, 2778, 2779, 2780, 2781, 2782, 2783, 2784, 2785, 2786, 2787, 2788, 2789, 2790, 2791, 2792, 2793, 2794, 2795, 2796, 2797, 2798, 2799, 2800, 2801, 2802, 2803, 2804, 2805, 2806, 2807, 2808, 2809, 2810, 2811, 2812, 2813, 2814, 2815, 2816, 2817, 2818, 2819, 2820, 2821, 2822, 2823, 2824, 2825, 2826, 2827, 2828, 2829, 2830, 2831, 2832, 2833, 2834, 2835, 2836, 2837, 2838, 2839, 2840, 2841, 2842, 2843, 2844, 2845, 2846, 2847, 2848, 2849, 2850, 2851, 2852, 2853, 2854, 2855, 2856, 2857, 2858, 2859, 2860, 2861, 2862, 2863, 2864, 2865, 2866, 2867, 2868, 2869, 2870, 2871, 2872, 2873, 2874, 2875, 2876, 2877, 2878, 2879, 2880, 2881, 2882, 2883, 2884, 2885, 2886, 2887, 2888, 2889, 2890, 2891, 2892, 2893, 2894, 2895, 2896, 2897, 2898, 2899, 2900, 2901, 2902, 2903, 2904, 2905, 2906, 2907, 2908, 2909, 2910, 2911, 2912, 2913, 2914, 2915, 2916, 2917, 2918, 2919, 2920, 2921, 2922, 2923, 2924, 2925, 2926, 2927, 2928, 2929, 2930, 2931, 2932, 2933, 2934, 2935, 2936, 2937, 2938, 2939, 2940, 2941, 2942, 2943, 2944, 2945, 2946, 2947, 2948, 2949, 2950, 2951, 2952, 2953, 2954, 2955, 2956, 2957, 2958, 2959, 2960, 2961, 2962,

banking associations, such owner may be treated, for the purposes of that section, as a shareholder and liable as therein prescribed." The case, however, is not directly in point.

The most pertinent in this connection is that of *Stuart v. Hayden*, 169 U. S. 1. In that case, Stuart, being an owner of one hundred shares of stock in a national bank, a director of the bank, and a member of its finance committee, purchased certain real property of Gruetter and Joers, and as a consideration assumed a mortgage debt, turned over his stock in the bank as of the value of \$18,000, delivered to them the certificate of the shares and paid the balance of the agreed price in cash.

These certificates of stock were returned to the bank and new certificates issued to Gruetter and Joers, to whom Stuart represented that the bank was in a solvent and prosperous condition. The Circuit Court found that such representation was false to the knowledge of Stuart, and made for the purpose of inducing them to purchase the stock, and of evading and escaping his liability as a shareholder for his assessment thereon. Upon this state of facts Stuart was held liable to the receiver as the holder and owner of these shares.

The principal inquiry was whether Stuart transferred his stock to escape the liability imposed by the statute, his contention being that, if the transfer were absolute and to persons who were at the time solvent and able to respond to an assessment upon the shares, the motive with which the transfer was made was of no consequence.

In answer to this it was said by Mr. Justice Harlan (pp. 7, 8):

"There is no case in which this court has held that the intent with which the shareholder got rid of his stock was of no consequence; certainly, no case in which the intent was held to be immaterial, when coupled with knowledge or reasonable belief upon the part of the transferrer that the bank was insolvent or in a failing condition.

* * * * *

"One who holds such shares—the bank being at the time insolvent—cannot escape the individual liability imposed by the statute by transferring his stock with intent simply to avoid that liability, knowing or having reason to believe, at the time of the transfer on the books of the bank that it is insolvent or about to fail. A transfer with such intent and under such circumstances, is a fraud upon the creditors of the bank, and may be treated by the receiver as inoperative between the transferrer and himself, and the former held liable as a shareholder without reference to the financial condition of the transferee."

The court found upon the facts (p. 14) "that Stuart, with knowledge of the insolvency of the bank, or at all events with such knowledge of the facts as reasonably justified the belief that insolvency existed or was impending, sold and transferred his stock with the intent to escape individual liability, . . . and the bank having been in fact insolvent at the time of the transfer of his stock—

which fact is not disputed—he remained the transferor, and as between the receiver and the transferee subject to the individual liability imposed by the statute, though it was alleged in the bill by the transferees that they were at the time of the transfer bona fide purchasers. There was no finding to that effect, and in *Stuart* no stress was laid upon their case. The case was disposed of as one of bad faith in transferring the shares at a time when he knew the company was insolvent. There is certainly nothing in this case to suggest that the receiver was bound in making out his report on the fact that the transferee was insolvent, or that the transferee was to be so when he transferred his shares.

In *Matteson v. Dent*, 176 U. S. 521, the stock was yet owned by him and stood in his name at the time of the intestate's death, and the stock was distributed by the decree of the Probate Court. Shortly after the death of the insolvent and the receiver brought suit against the children for an assessment. [The defendant pleaded] on the ground that the obligation of a stockholder is contractual in its nature, and is not extinguished by the insolvency of any other contract obligation, survives as a debt of the estate of the stockholder, notwithstanding the death of the decedent had been settled and fully administered, and that the insolvency of the bank occurred after the death of the intestate, citing *Richmond v. Irons*, 121 U. S. 193. The case did not involve the question here presented. In the opinion the prior cases of *National Bank v. Atchafalaya* and *Bowden v. Johnson*, 107 U. S. 251, were cited, and the proposition, treated as elementary, that if the stock has been fraudulently or collusively made to avoid assessments, such transfer will be disregarded and the transferor held liable." (p. 531).

Much stress is laid, in the opinion of the court, upon the fact that in the case of *Earle v. Carson*, 188 U. S. 416, the receiver was bound to establish the fact that the transferee was not a bona fide purchaser to establish the fact that the transferee was not the transferee to be so at the time of the transfer. It was that, prior to the suspension of the receiver, the good faith sold the stock standing in her name for the price, which had been paid her; that she had received her stock certificate, with a power of attorney, and requested that the stock be transferred to the bank. The bank said the transfer would be made, but the bank had failed to discharge that duty; that the receiver had everything which the law required her to do, and she had ceased to be a stockholder and was not to be alleged as error that the trial court refused to set aside the verdict.

the sale of the stock, though lawful in every other respect, could not be so treated if it were found that at the time of the sale the reserve of the bank were, to the knowledge of the defendant, below the limit fixed by law (p. 44). This refusal was held not to be an error. "Certainly," said Mr. Justice White in the opinion (p. 46), "it cannot in reason be said that the power would exist to sell stock like any other personal property if before the power could be exercised the seller must examine the affairs of the bank, marshal its assets and liabilities in order to form an accurate judgment as to the precise condition of the bank."

In discussing the question in regard to the validity of the transfer, it was said (p. 49) that "the exercise of the power to transfer stock in a national bank is controlled by the rules of good faith applicable to other contracts. The qualification just stated gives no support to the proposition that where a sale of stock in a national bank is made in good faith, nevertheless the consequences of the sale are avoided if subsequently it developed that the bank was insolvent at the time of the transfer, in the sense that its assets were then unequal to the discharge of its liabilities, when such fact was unknown to the seller of the stock at the time of the sale."

The argument was made (p. 54) that as the "person to whom the stock was sold was insolvent, and hence unable to respond to the double liability, the sale was void, although the fact of such insolvency of the buyer was unknown to the seller." This was held to be unsound, "since it but insists that the validity of the sale of the stock is to be tested, not by the good faith of the seller, but upon the unknown financial condition of the buyer." We find nothing in this case which impugns in any degree the authority of the prior cases, or holds that the validity of the sale is to be gauged by the financial condition of the transferee, or the knowledge of that condition by the transferor.

1. We think it a proper deduction from the prior cases, and such we hold to be the law, that the gist of the liability is the fraud implied in selling, with notice of the insolvency of the bank and with intent to evade the double liability imposed upon the stockholder by the National Banking Act. In short, the question of liability is largely determinable by the presence or absence of an intent to evade liability. The fact that the sale was made to an insolvent buyer is doubtless additional evidence of the original fraudulent intent, but would not be in itself sufficient to constitute fraud without notice of the insolvency of the bank. The stockholder is not deprived of his right to sell his stock by the fact that the sale is made to an insolvent person, unless it be made with knowledge of the insolvency of the bank. This was practically the ruling in *Earle v. Carson*, in which we held that a *bona fide* sale would not be void, though the vendee were insolvent, if the fact of such insolvency were at the time unknown to the seller. The case of *Earle v. Car-*

son, so far from lending countenance to the vendees, bears strongly in the opposite direction.

The solvency of the vendee, however, is not a defense, that no damage could have resulted to the plaintiff by the transfer. Though not a necessary part of the case, it may be a complete defense, if it be shown that the transfer was made to a vendee who was not liable as stockholder. The double liability as was the vendor. The vendees are not responsible because the vendees, being defensive in its character, upon them. In this particular the case is a primary action upon a contract, where the plaintiff transfers the stock and the breach, and sues for such damages as he is entitled to follow therefrom. But it is not shown that no damages really resulted, as, for instance, that plaintiff might have obtained the same wages, or in an action for a failure of the vendee, plaintiff might have gone into the market at the same price at which the defendant sold. In such case defendant assumes the burden of showing that no damage in fact resulted. The argument is that the receiver was bound to show, not only that no fraud, but that damages necessarily resulted from that fact. The reply is that the fraud was of the stock of a bank known to be insolvent at the time of the transfer, and that the fraud is not less the cause of the damage than the fact that the bank was insolvent to be solvent, but that their solvency was the presumption that injury resulted to the plaintiff by the transfers.

While there is no express finding of the fact (as there was in the Circuit Court) that Dewey was not a stockholder, of the insolvency of the bank at the time of the transfer, and that the transfer was made with the intent to defraud the creditors, the decree of both the Circuit Court and the Supreme Court is based upon the assumption; and as stated in the dissenting opinion, "the suspension of the bank, though it occurred several months after Dewey's transfer of stock, is the cause and effect, to the insolvency of the bank at the time of the transfer." We do not understand these facts to be disputed.

In this connection it only remains to consider whether the vendees were financially responsible to the plaintiff. It is not necessary to show that they were financially equal to that of the original stockholder. It is sufficient to show that they were responsible to the amount called for in the case—in other words, in an amount sufficient to satisfy the creditors of the bank were not damnified by the transfer.

Although the evidence does not show affirmatively the insolvency of the ultimate transferees, it falls far short of showing that a decree against them for their assessment could be collected. Without going into details of the property of each one of the seven transferees, it is sufficient to say that they were either working on salaries, with no evidence of available property, outside of such salaries, or that their property consisted of incumbered real estate in Chicago of a largely speculative value; and that in some cases, at least, the shares were paid for in real estate conveyed for the purpose of getting rid of the property and avoiding the payment of interest on the incumbrances. There is no satisfactory evidence that a decree against any one of these parties for the amount of his assessment could have been collected by ordinary process of law.

2. But, except so far as the twenty-five shares held by Jewett as the agent of Dewey at the time of the failure, we think the executors should not be liable to the creditors who became such after the transfer. The National Banking Act requires (Rev. Stat. § 5210) a list of the names and residences of all the shareholders, and the number of shares held by each to be kept in the banking house, subject to the inspection of all the shareholders and creditors of the association; and (sec. 5139), that every person becoming a shareholder by a transfer of shares to himself shall succeed to all the rights and liabilities of the prior holder of such shares, and no change shall be made in the articles of association by which the rights, remedies or securities of the *existing creditors* of the association shall be impaired.

The object of this legislation is evidently to apprise persons dealing with the bank of the names of the shareholders, upon whom the double liability shall be imposed in case of the insolvency of the bank. In the event of such insolvency it is only existing creditors who can claim to have been damnified by a fraudulent transfer of shares. As to them such transfer is voidable. Subsequent creditors are apprised by the published list of the names of the shareholders, to whom transfers have been made, and of the persons to whom they have recourse for the double liability. The injustice of holding a stockholder liable for an indefinite time in the future to creditors who may have become such years after he had parted with his stock, and who were apprised of the names of the stockholders by the published list, is too manifest to require an extended comment. We are only applying to this case by analogy the ordinary rule of the common law, that a voluntary deed by a person heavily indebted is fraudulent and void as to prior creditors merely upon the ground that he was so indebted, but as to subsequent creditors is only void upon evidence that the deed was made in contemplation of future indebtedness. *Sexton v. Wheaton*, 8 Wheat. 229; *Schreyer v. Scott*, 134 U. S. 405; *Ridgeway v. Underwood*, 4 Wash. C. C. 129, 137; *Bennett v. Bedford Bank*, 11 Massachusetts, 421.

This was the interpretation given to a similar statute by the Su-

preme Court of Ohio in *Peter v. Union*, 107 Ohio 204. It is true that in Ohio a stockholder is liable to existing creditors by a transfer of his shares, but such transfer may be. But we do not see in the *Peter* case, that he does not continue liable to creditors.

The case of *Bowden v. Johnson*, 107 Ohio 204, is a question of the fraud in a certain transfer, being that such transfer was fraudulent, and whether such liability was limited to existing creditors or to future creditors was not touched upon, but as the insolvency of the bank seems to have existed at the time the fraudulent transfer was made, it is not surprising that creditors existed.

There are, undoubtedly, cases in which the expression that in the event of a fraudulent transfer a stockholder remains liable to the creditors of the corporation is called upon to discriminate between subsequent creditors, since as a rule the corporation is liquidated soon after the transfer, and the decision is left to our attention by counsel.

It results that there must be a decree of the Circuit Court of Appeals so far as it holds the stockholder liable for assessment on the twenty-five shares sold and reversing in so far as it exonerated the stockholder upon the remaining shares to such amount as the creditors existing at the time the transfer was made, and that the cause be remanded to the Northern District of Illinois for further consideration of this opinion.

MR. JUSTICE WHITE, with whom concurred MR. JUSTICE DAY, dissenting. * *

Besides to me it seems that the rule announced is self-destructive. What is the liability imposed? Is it a responsibility only to pay the debts existing at the time a fraudulent transfer was made? Is the only liability imposed by the statute an obligation to respond to an equal and similar obligation of the Comptroller to pay the debts existing at the time of the failure? Rev. Stat. Secs. 5151, 5234. From this it follows that if a stockholder at the time of the failure is not a stockholder at the time of the failure, and if he is such stockholder he is liable for the debts existing at the time of the failure no other. This plain result of the statute is the error of the conclusion as to limited liability. For, if Dewey was not a stockholder at the time of the failure, there is an entire absence of statutory authority for his liability.

whatever upon him, and if he was such stockholder then the statute fixed the measure of liability, and there is no power to substitute by judicial discretion a liability which the statute does not impose, and which on the contrary is excluded by its express terms. In other words, the statute imposes a uniform and ratable liability upon all stockholders who are liable at all and affords no justification for assessing one stockholder at one amount and another stockholder in another sum, upon the theory that the date of the contracting of debts and not the date of the failure is the test of liability.

And that this departure from the long received and judicially sanctioned construction of the statute will tend to destroy the security of the national banking system by rendering the double liability impossible of enforcement results from a few obvious considerations. Thus, under the rule now announced, one who owns or controls a majority of the stock of a national bank, knowing it to be insolvent, can transfer his stock to wholly irresponsible persons in order to avoid the statutory liability, and, by postponing the date of open failure until the existing debts of the bank have been extinguished by novation, leave the creditors existing at the time of failure with substantially no stockholder to respond to the double liability. Indeed, this condition of things cannot be more cogently made manifest than by considering the facts in this case as found by the court. What are they? They are that Dewey was an officer of the bank and knew its hopelessly insolvent condition, and that he transferred his stock to avoid the liability, leaving the shares in the name of his agent or causing that agent to put the same in the names of irresponsible people. In effect controlling the affairs of the bank, Dewey delays the open failure until by a change of the situation, although the indebtedness of the bank may not have diminished, yet, by a mere substitution of creditors, the particular debts due at the time of his fraudulent transfers have largely been extinguished. And thus, when the open failure comes, it is now decided that, as to the shares fraudulently transferred by his agent, Dewey owes nothing toward payment of the debts of the bank, except as to debts still existing, which were contracted prior to the fraudulent transfers. In other words, it is held that although the bank was insolvent prior to and at the time of the commission of the fraudulent acts and continued so to the time of the failure, the fraudulent transferrer has accomplished the wrong which the statute was intended to prevent by holding back and preventing the open failure until he had discharged, at the expense of the subsequent creditors of the bank, the indebtedness existing at the time of the fraudulent transfers. Under the rule hitherto prevailing the duty of the administrative officer was plainly marked out in the statute, to realize the assets, and, if necessary to meet a deficiency of assets, to assess ratably the legal stockholders—a simple and effective rule. Now the duty of the administrative officer is wholly changed. He must analyze the situation at the bank, he must determine who were

creditors at this time and that, in order to protect the interests of the stockholders, and when this process is gone through, the equal and ratable statutory liability of the stockholders for unequal and unratable claims of the creditors.

I can see no reason for now changing the National Banking Act as applied in former cases, as embodied in the text and spirit of the Act, by a long line of decisions of this court, the probable consequence of such change will, in the end, be to the detriment of the public interest and the interests of national banks which it was the purpose of the Act to secure.

It remains only to briefly notice the case of *Bank of Ohio v. Wabash*, 56 Ohio St. 181, heretofore referred to in its opinion. To understand that case, it is necessary to refer to the opinion of the Supreme Court of Ohio, *Brown v. Hitchcock*, 10 Ohio St. 201, in which the opinion in the Peter case was taken into view. In *Brown v. Hitchcock*, the Supreme Court of Ohio held that by the constitution and laws of that State a stockholder who was subjected to a double liability on his stock, however *bona fide* might be the owner, so as to escape liability to creditors who were not transferred. In other words, the court held that the double liability imposed by the Ohio statute was not efficacious transfer of the stock without the consent of the creditors, since such creditors, despite a *bona fide* transfer, remained unsatisfied, and were not required, to proceed against the stockholder at the time the debt was contracted, and that the corporation was at the time of the transfer. Subsequently, in the Peter case, the Ohio court determined how far a transfer of stock by an Ohio corporation operated to relieve him from liability to the corporation. As to this question the court in the Peter case cited the Ohio statutes the English "out and out" rule, whilst reiterating its ruling as to the fact that a stockholder who made an out and out transfer of his stock to a corporation was insolvent and the purpose of the transfer was to escape liability, was discharged from any responsibility to existing creditors, although remaining liable to existing creditors between the Ohio statutes, as thus expounded by the National Banking Act, as expounded by this court, by the statement that under the National Banking Act, a stockholder, as repeatedly decided by this court, in good faith, to dispose of his stock and the proceeds thereof to existing and future creditors, and that the National Banking Act, as applied to future debts, applied to

statute of that State, was expressly repudiated by this court as to the National Banking Act in the Case and subsequent decisions. To treat then, the Ohio case as authoritative here, is, in effect, but to expunge the National Banking Act from the statutes of the United States and to substitute in its stead the statutes of Ohio, when such statutes have a wholly different significance as interpreted by the highest court of that State.

*I therefore dissent.**

WHITE CORBIN & CO. v. JONES.

1901. 167 N. Y. 158, 60 N. E. 422.

APPEAL from a judgment of the Appellate Division of the Supreme Court in the fourth judicial department, entered December 1, 1899, affirming a judgment in favor of plaintiff entered upon a verdict and an order denying a motion for a new trial.

The nature of the action and the facts, so far as material, are stated in the opinion.

HAIGHT, J.—This action was brought by the plaintiff, as a judgment creditor of the Rochester Lithographing and Printing Company, a corporation organized under chapter 40 of the Laws of 1848 and amendments thereto, to recover of the defendant, a stockholder, upon the ground that the capital stock of the corporation had not been fully paid in.

The corporation was organized on the 5th day of May, 1887, with a capital stock fixed at \$50,000, divided into five hundred shares of one hundred dollars each. The defendant was not an original stockholder, but in February, 1888, he purchased stock from one of the stockholders of the corporation and thereby became a member of the company. On the 28th of April, 1889, a certificate was filed in the office of the clerk of the proper county to the effect that the capital stock of the company had been fully paid, and this certificate was duly recorded as required by the statute. Subsequently, and in December, 1889, an assessment was levied upon the stock of the corporation, from which the sum of \$6,500 was collected and paid into the treasury of the company. The plaintiff's claim was contracted thereafter. It appears that before the organization of the corporation there was in existence a firm known as Willard, Pitt & Moore, engaged in the lithographic business in Rochester, and also another firm known as Goble & Vredenburg, engaged in the printing business. Each of these firms had plants, machinery, stock and property for the conduct of their business. These firms arranged to consolidate and organize a corporation. The Rochester Litho-

* See *Rochester & Kettle Falls Land Co. v. Raymond*, (1899) 158 N. Y. 576, 53 N. E. 507, 47 L. R. A. 246; *Sinclair v. Fuller* (1899) 158 N. Y. 607, 53 N. E. 510. See also, *Cook, Corps.* (6th ed.) §§ 263-266.—Eds.

graphing Company was thereupon organized, and these companies were sold to the corporation, and the claim is that the plants and companies were put into the corporation at an overvaluation by reason of such overvaluation the corporation was fully paid.

The evidence upon the trial was of such a nature that the jury might have found that the overvaluation was not more than \$6,500. At the conclusion of the evidence the jury, among other things, that "In my opinion, it makes no difference with the law whether he knew of this overvaluation or not, whether there was an intentional and substantial misstatement of property by these trustees at the time when the overvaluation was done for the purpose of evading the statute, then, unless the error was corrected by such a payment as would make up the deficiency of the defendant as well as of any other stockholders, in regard to the knowledge which he or they had of the transaction. It is due, however, to the defendant that he was not charged that he had any personal knowledge of the overvaluation of the property which was owned by Vredenburg and by Pitt to the corporation, as you will remember, was not a member until February, 1901, and was then asked by the defendant to charge the jury that he did not find from the evidence in this case that the overvaluation of the property which was owned by Vredenburg and by Pitt to the corporation did not exceed \$6,500, and that the payment made by the corporation subsequently paid into the treasury upon their stock for the promotion of the corporation cured the error of which the trustees were guilty in the overvaluation of the property at such overvaluation." This exception was taken by the defendant and was sustained also to the refusal to charge as requested.

The statute under which the Rochester Manufacturing Company was organized provides as follows:

"§ 10. All the stockholders of every corporation organized under this act, shall be severally individually liable for the debts of the company in which they are stockholders, in proportion to the amount of stock held by them respectively, until the whole amount made by such company, until the whole amount of the capital stock and limited by such company shall have been paid, and certificates thereof shall have been made and filed in the office of the following section; and the capital stock shall be paid in, one-half thereof within one year, and the other half thereof within two years from the incorporation, or such corporation shall be dissolved.

"§ 11. The president and a majority of the stockholders of every corporation organized under this act, shall be severally individually liable for the debts of the company in which they are stockholders, in proportion to the amount of stock held by them respectively, until the whole amount made by such company, until the whole amount of the capital stock and limited by such company shall have been paid, and certificates thereof shall have been made and filed in the office of the following section; and the capital stock shall be paid in, one-half thereof within one year, and the other half thereof within two years from the incorporation, or such corporation shall be dissolved.

days after the payment of the last installment of the capital stock, so fixed and limited by the company, shall make a certificate stating the amount of the capital so fixed and paid in; which certificate shall be signed and sworn to by the president and a majority of the trustees; and they shall, within the said thirty days, record the same in the office of the county clerk of the county wherein the business of the said company is carried on."

The provisions of the statute are very broad. They in terms cover all the stockholders of the corporation, and they are made severally and individually liable to the creditors until the capital stock is paid in, and a certificate by the president and a majority of the trustees is made and recorded in the office of the clerk of the county. We incline to the view (that persons contracting with a corporation, by which they give credit to it, have the right to rely upon the liability of all the stockholders, and not a portion thereof, until the certificate is given; and that persons becoming stockholders before the stock is paid in, and a certificate given, must be understood as contracting that they will be personally liable to creditors to an amount equal to the stock held by them until the terms of the statute are fulfilled. It may be very different with persons who have acquired stock in a corporation after the certificate has been made and recorded. As to such persons they may have the right to rely upon the truthfulness of the certificate, and, possibly, they do not become liable under the provisions of this statute; but the defendant acquired his stock before the certificate was made and recorded, and although he may not have known of the overvaluation, we think he became bound under the terms of the statute and that the charge as made was correct.

We, however, have difficulty with the exception taken to the refusal to charge as requested. Assuming that there had been an overvaluation, and that there had subsequently been an assessment paid in by the stockholders of an amount equal to such overvaluation, it appears to us that the defect was cured as to all creditors whose claims thereafter accrued. If this is not so, we know of no way in which the stockholders of a corporation could relieve themselves from the liability created by the misconduct of the original trustees, even though the offending stockholders had ceased to be members of the corporation and their stocks had been acquired by innocent purchasers for value. It is said that the assessment was not made for the purpose of completing the payment of the capital stock left unpaid in consequence of the overvaluation of the property purchased. It was made, as we understand, for the purpose of increasing the amount of money in the treasury of the corporation. This, of necessity, had the effect to increase the cash capital of the company, and if it equalled the amount of the capital stock unpaid it is not apparent how it could be thereafter claimed that the stock had not been paid for in full. Nor do we think that the postponement of the assessment until after the expiration of two years from the

organization of the corporation affects general might have instituted proceedings, but he did not, and he is not heretaken by the corporation. The purpose of protection of creditors, and it is not apparent would have proved a greater protection to the subsequent creditors. We, consequently, that the requests should have been charged.

The judgment should be reversed and the costs to abide the event.*

HIGGINS v. ILLINOIS TRUST A

1901. 193 Illinois 394, 6

MR. JUSTICE HAND delivered the opinion

A bill in chancery was filed on January 1, 1901, by Morse, a judgment creditor of the Pacific circuit court of Cook County, in behalf of the stockholders of said company, under Section 32 of Hurd's Stat. chap. 32, against said company to enforce the statutory liability of said company to balance upon their stock. * * *

The main question presented by this case is whether the stockholders are liable by creditors to wind up an insolvent corporation with the balance due on unpaid stock. The assignor of assessed stock shall respond to the assessment made by the court thereon.

The general rule is, that the assignee of the rights and assumes all liabilities of the corporation in its insolvency of the corporation is liable to the creditors of the corporation to the extent that the stock issued has been issued as fully paid and the same in good faith and without notice that he is not liable to the creditors of the corporation to the extent of the balance due upon the stock. (3 Thompson 322; Kellogg v. Stockwell, 75 Ill. 68; 316; Coleman v. Howe, 154 id. 458; Sprague v. Webster v. Upton, 91 U. S. 65.) Nor is Section 8 of the Corporation act, which only binds signors and assignees to the corporation. In the section from Thompson on Corporations it is said: "The transferee succeeds not only to the rights but also to the liabilities of the transferer. * * *

* See West Nashville Planing-Mill Co. v. Nashville, Tenn., 252, 6 S. W. 340, 6 Am. St. 835; Rowell 60 at p. 66, 45 N. E. 398.—Eds.

solvency of the corporation he is liable to contribute to the payment of its debts in like manner as if he were an original subscriber." In *Coleman v. Howe*, 154 Ill. 458, we say (p. 471): "A purchaser or assignee of stock which has not been fully paid does not become liable to the corporate creditors for the unpaid balance, where the stock has been issued as fully paid and he has acquired the same in good faith and without notice that it has not been fully paid."

The stock in question was issued as fully paid, and, it may be conceded, was acquired in good faith. Was it acquired without notice that it was not fully paid? We think not. The plaintiff in error and his vendors were stockholders in the cable company, knew the objects for which the Pacific Railway Company was organized, and exchanged their stock in the cable company for stock in the Pacific Railway Company, share for share. As no stock was issued by the Pacific Railway Company except in exchange for cable company stock, and as the entire stock of the Pacific company was issued and exchanged for cable company stock without any further payment therefor, and the plaintiff in error paid only \$32 a share for the stock which he received directly from the Pacific Railway Company a short time before he purchased said stock, he must be held to have purchased such stock with notice that it was not fully paid. At the time of the sale of said stock there were no representations made to the plaintiff in error by said assignors, or either of them, that the same was full paid stock, and it is apparent that the stock was purchased by plaintiff in error upon his own knowledge of the stock, which was equal to that of the assignors or either of them, and not by reason of the fact that the stock certificates stated "this stock is full paid and non-assessable." The plaintiff in error may have thought the stock was non-assessable. He knew, however, it was not full paid stock. (The fact, therefore, that the stock was stated to be full paid did not amount to a warranty which would relieve the plaintiff in error from the payment of an assessment thereon.) Neither does the fact that both the assignees and assignors were owners of cable stock, which they had exchanged for Pacific Railway stock at or about the time it was organized, estop the creditors of the corporation or the assignors from insisting that plaintiff in error be held primarily liable for such assessments. The assignors, by the sale of such stock, warranted to the assignee that the same was genuine; that they were the owners thereof and authorized to transfer the title thereto. If the assignee desired anything further he should have exacted a special guaranty for his protection. *First Nat. Bank of Sterling v. Drew*, 191 Ill. 186.

Under the authority of *Florsheim v. Illinois Trust and Savings Bank*, 192 Ill. 382, the court did not err in allowing interest from October 1, 1898, on said assessments.

Finding no reversible error in this record the judgment of the Appellate Court will be affirmed.

*Judgment affirmed.*⁵

⁵ See *Waterhouse v. Jamieson* (1870) L. R. 2 H. L. (Sc.) 29.—Eds.

CHAPTER X.

PROMOTERS. UNDERWRITING.

IN RE BRITISH SEAMLESS PAPER BOX CO.

1881. L. R. 17 Ch. Div. 467.¹

JESSEL, M. R.—I do not think it necessary to hear the Respondents as they do not ask for costs.

First of all, as far as I know, there is no case like this. If there were, I should only be too glad to follow it. It is an entirely new case, and entirely distinguishable from that of the *Society of Practical Knowledge v. Abbott*, 2 Beav. 559, before Lord Langdale, which was a very peculiar case. It was simply this: The company was a chartered company, and by the terms of the charter the shares were to be paid for in cash, and in no other way. The four gentlemen who obtained the charter allotted the shares to themselves without paying for them in cash, and sold them to other people, and then the corporation sued them for the balance of cash due on their allotments. Lord Langdale held that, having regard to the terms of the charter of the corporation, these four gentlemen had no right to allot the shares to themselves except for cash, and therefore that the claim made by the bill was well founded.

That case does not appear to me to have the slightest application to a company formed as this is. The other case of *New Sombrero Phosphate Company v. Erlanger* appears to me also to have no application. I quite agree to this, that if promoters make an arrangement to get a profit for themselves out of what is apparently paid to the vendors, it is immaterial whether the contract with the vendors is approved of by the directors of the company, who are the promoters, just before the allotment or just after: in both cases it is intended to cheat the future shareholders; and of course it makes no difference whatever that the persons who, at the time the allotment was made, were in fact the promoters or their nominees, knew of the fraud. You can defraud future allottees as well as present allottees. Therefore that case appears to me to have no direct bearing upon the case before me.

¹ The facts sufficiently appear in the opinion of Jessel, M. R. The opinions of Brett, L. J. and Cotton, L. J. are omitted.—Eds.

What, then, is this case? I must say I am convinced of the thorough honesty of all parties engaged in the transaction. Of course, to a certain extent, the honesty of the parties engaged in a particular transaction must naturally affect the case in the mind of the Judge who has to consider the transaction; but, as far as I am concerned, I always endeavor to administer justice fairly, according to law, even if it should bear hardly on people, as it sometimes does. I say "fairly," because my mind is affected—as every Judge's mind must be affected—to some extent, at all events, by what I will call the "morality" of the transaction. I should be more anxious to find reasons to trounce a rogue than I should be to find reasons to rob an honest man.

The present question is this: Three Americans, who appear to be inventors, were possessed of a certain patent. Whether it is valuable or not I do not know—it has not been successfully worked in this country; but it was supposed to be valuable. An English engineer of the name of Ransome appears to have had some faith in it; at all events, he agreed to advance £2,000 for the purpose of introducing a machine into this country to make seamless paper boxes according to the patent. This he agreed to do under an agreement in writing of a very curious character, and the effect of which it is very difficult to state in a few words. The agreement is dated the 7th of January, 1874. In substance it was this, I think: that he was to advance £2,000 to get the machine at work; if he got it to work satisfactorily the company was to be formed, he was to get £2,000 worth of shares for his £2,000 advanced, the three Americans were to get £30,000 in shares out of a total capital of £50,000, and out of those shares Mr. Ransome was to receive £6,000; but if the machine turned out a failure, and through no fault of Mr. Ransome's, he was then to be entitled to have a fifth of the patent. So that the moment this agreement was signed Mr. Ransome was to be treated as substantial owner of one-fifth part of the patent. That was the substance of the agreement.

Then a meeting of the promoters was called, at which three other gentlemen were present. They divided the interest with the Englishman, and they agreed to get up a company on the footing of this agreement of 1874; they not only knew all about it, but their arrangement was to form a company on that footing; and it having been arranged to form what I will call for this purpose a private company—for it was not intended to come before the public at all—a formal agreement, not a real agreement, was made on the 27th of February, 1875, between the three Americans of the one part, and a Mr. Bennett, who was their nominee, of the other part, for the nominal sale to the company of the patents for £32,000 in shares. Of course this was a mere bit of form, with the view of launching the company. The company was registered on the 4th of March, and contemporaneously they prepared a memorandum of association to carry out the formal agreement, with articles of association mak-

ing all the members of the company directors, with the exception of the solicitor, who knew all about the formation of the company and was the only additional person who came in to sign the memorandum of association. The result was that, at the time of the formation of the company, the company consisted of eight men, and it was not intended to consist of any more. There was power, of course, to issue the remainder of the shares, but the intention of these eight men was to carry on the company with these shares, and accordingly we find this, that there is a meeting of directors after the company is formed, ratifying the formal agreement of 1875 and allotting the shares, and allotting them on the principle of recognizing the agreement of 1874, of which they were all aware, and which is actually mentioned by its date in one of the early meetings of the directors; so that they recognize Mr. Ransome's right to be treated as one of the vendors, and to be paid his share of the purchase-money.

That being so, it appears—though not so clearly as might be—that the other directors thought that Mr. Ransome had incurred expenses to the extent of £3,000; but when they found that he had only paid £2,000, they insisted that the other £1,000 should be applied by him in taking up £1,000 worth of shares, which he did; and then, again, a few days after the formation of the company, it seems that five shares apiece extra were given to the Messrs. Stevens (I will assume that it was a bonus), apparently with the knowledge of everybody, in consideration of their having furnished the capital, which they in fact did.

Now, if this company had been intended to be formed as a company in which the shares were to be taken by the public, and a prospectus had been issued immediately after these transactions, concealing them from the allottees, and the allottees had come in, and afterwards, with reasonable promptitude, repudiated the contract, I think a great deal could have been said in favor of their contention, but that is not the case. The company went on, as they intended to go on, with these eight people. In 1875 there is a regular general meeting of the company, and the seal of the company is put to the register of shareholders, treating it as then complete. I then find another regular meeting of shareholders held on the 30th of June 1876, and at that time there are still only eight shareholders, so that the position of the company up to June, 1876, was this, that every member of the company was perfectly well aware of the whole of the transaction. It was confirmed in March, 1875, and the members carried on business for the whole period—that is, from March, 1875, to June, 1876—without attempting to repudiate the transaction, even if they could have repudiated it.

What then was the position of the company—not the promoters only—as regards the vendors and as regards Mr. Ransome? They are actually the same people with the exception of Mr. Tindell, but the company itself had adopted this contract of 1874 with full

knowledge of every member of it (which is a case I never heard of before), without any intention of bringing in any other shareholder, without any notion of defrauding any future allottee, and had made this bargain with knowledge of the facts. Is it possible to say that the company is not bound by that? It would be impossible to say so. The transaction was entirely bona fide in every respect.

What occurred subsequently was this: In June, 1876, the company wanted more capital: Messrs. Stevens and other English shareholders were willing to contribute a little more, but not enough; five gentlemen, who were strangers, then came in and joined the company, and they had an allotment of shares to a considerable amount no doubt, but not to a large amount. I agree it would have been right that the agreement of 1874 should have been stated in the memorandum and articles of association, and that is one reason why I am not disposed to give costs to these gentlemen, because I think their neglect in not so stating it has induced the liquidator to make this application; but, even assuming (and this is a point upon which I give no opinion, because I have not heard the evidence fully) that the people who subsequently came in did not know what the original transaction was, they would have no right to bring an action on the facts, and say they were thereby induced to become members of the company; that is, if they were defrauded at all. I give no opinion as to what their state of knowledge was, because there is a conflict of evidence about it; but I can not see that that would make those persons guilty of misfeasance who had actually entered into a contract with a bona fide company carrying on business, every article of which contract was known to every member of the company.

It appears to me that on the 30th of June, 1876, the company, having acted on the contract with that knowledge, the subsequent allotment of a portion of the shares not being part of the scheme originally contemplated, were not bound to alter the relations between the company and their vendors, and consequently that this application which is made by the liquidator under the 165th section of the Companies Act, 1862, must fail.

From this judgment the official liquidator appealed.

JAMES, L. J.—It appears to me that the Master of the Rolls has really put the matter on the true footing in that passage of his judgment in which he makes the question resolve itself into one of honesty or dishonesty. He was of opinion, and I agree with him, that the directors were, and intended to be, thoroughly honest, and that they were, and intended to remain, the sole proprietors of the property of the company and the sole members of the company, and that whatever agreements they chose to make among themselves as to the division of the property, concerned themselves alone. That being so, it distinguishes this case from the case of the Society of

PROMOTERS.

Practical Knowledge v. Abbott, because anything like a bonus has been given to in question by allottees of shares, the bur those who have received it, to satisfy t tended to be and was in fact honestly r tending, although then constituting the v people should come in afterwards to w would be injurious, the Court would feel Lord Langdale did in the Society of Pr bott, 2 Beav. 559, that they intended to co was nothing of that kind. That is the gr of the Rolls, and I concur in his opinion. sion in favor of these directors may open tices in future. But I think we ought no for an action in order that it may disco doing something like it. The appeal mus

GLUCKSTEIN v. BA

1900. L. R. (1900) A.

EARL OF HALSBURY, L. C.—My Lord question is whether four persons, of w can be permitted to retain the sums whic the company of which they were directo tence that they had paid 20,000l. more th for property which they, as a syndicate, b among themselves, and then sold to then company. If this is an accurate account these four persons, of course so gross a mitted to stand. That that is the real n to shew.

In the year 1892 the freehold ground "Olympia" were the property of a compa being wound up. That company had iss tent of 100,000l. as a first charge and charge for 10,000l. The four persons i property would have to be sold, and th order that they might resell it to a compa selves. The combination, which called i cate, but which, perhaps, the common l

¹ Cf. Society of Practical Knowledge v. Abbe Ambrose Lake &c. Min. Co. (1880) L. R. 14 Ch v. Spooner (1889) 74 Wis. 307, 42 N. W. 259, 17

² The opinions state the facts. Portions of opi

by a less high-sounding title, proceeded to buy up so far as they could the incumbrances on the property called "Olympia." They expended 27,000*l.* in buying debentures. These, of course, were very much depreciated in value, and they gave 500*l.* for the mortgage of 10,000*l.* As soon as this transaction had been completed they, partners in it, proceeded to form a company, and it was of course necessary that the company should be willing to help, and accordingly the four persons in question were made by the articles of association the first directors.

The property was sold on February 8 by the chief clerk of North, J., for 140,000*l.*, and the syndicate purchased nominally for that sum, but, by reason of the arrangement to which I have referred, that sum was less by 20,734*l.* 6*s.* 1*d.* than what they appeared to give. On March 29 they completed as directors the purchase of the property for 180,000*l.*, and they as directors paid to themselves as members of the syndicate 171,000*l.* in cash and 9,000*l.* in fully paid-up shares—in all 180,000*l.*

The prospectus by which money was to be obtained from the public disclosed the supposed profit which the vendors were making of 40,000*l.*, while in truth their profit was 60,734*l.* 6*s.* 1*d.*, and it is this undisclosed profit of 20,000*l.*, and the right to retain it, which is now in question.

My Lords, I am wholly unable to understand any claim that these directors, vendors, syndicate, associates, have to retain this money. I entirely agree with the Master of the Rolls that the essence of this scheme was to form a company. It was essential that this should be done, and that they should be directors of it, who would purchase. The company should have been informed of what was being done and consulted whether they would have allowed this profit. I think the Master of the Rolls is absolutely right in saying that the duty to disclose is imposed by the plainest dictates of common honesty as well as by well-settled principles of common law.

Of the facts there cannot be the least doubt; they are proved by the agreement, now that we know the subject-matter with which that agreement is intended to deal, although the agreement would not disclose what the nature of the transaction was to those who were not acquainted with the ingenious arrangements which were prepared for the entrapping the intended victim of these arrangements.

In order to protect themselves, as they supposed, they inserted in the prospectus, qualifying the statement that they had bought the property for 140,000*l.*, payable in cash, that they did not sell to the company, and did not intend to sell, any other profits made by the syndicate from interim investments.

Then it is said there is the alternative suggested upon the agreement that the syndicate might sell to a company or to some other purchaser. In the first place, I do not believe they ever intended to

PROMOTERS.

sell to anybody else than a company. might ask inconvenient questions, and if had stated as an inducement to an individual was given for the property, when been given, it is a great error to suppose enough to reach such a statement; but as was ever intended to get an individual intention would have had any operations towards sell to a company, they took very be no one who could ask questions. They themselves as buyers, and it was a necessity that they were to be both sellers and buyers the money to pay for the purchase from shareholders.

My Lords, I decline to discuss the question of the company. It is too absurd to suggest that to this transaction is a disclosure to the directors were the proper guardians and by the terms of the agreement to do that that is to say, to cheat the shareholders be treated as a disclosure to the company there to hoodwink the shareholders, and them, were to obtain from them the means of their nefarious plans.

I do not discuss either the sum sued for or the sum is sued. The whole sum has been obtained and all who were parties to it are responsible for what they have obtained and withheld from the shareholders.

I move your Lordships that the appeal be dismissed.

LORD MACNAGHTEN.—My Lords, Mr. Gluckstein has made an appeal with his usual ability, but the case is not a strong one. The learned counsel for the appellants have raised the slightest doubt in the mind of the majority of the judges to the propriety of the judgment under which the appellants were found with the learned judges of the Court of Appeal to venture to criticize their judgment at all, the defences put forward on Mr. Gluckstein's behalf were of no ceremony. For my part, I cannot see any fault in the trick which Mr. Gluckstein arranged to play on the persons whom they invited to take part in the transaction. It is the old story. It has been done before.

These gentlemen set about forming a company to raise a handsome sum for taking off their hands. They had contracted to buy with that end in view a piece of property into existence by means of the use of the company point themselves sole guardians and protectors of their interests, half-fledged and just struggling in the world.

foot while yet unborn by contracts tending to their private advantage, and so fashioned by its makers that it could only act by their hands and only see through their eyes. They issue a prospectus representing that they had agreed to purchase the property for a sum largely in excess of the amount which they had, in fact, to pay. On the faith of this prospectus they collect subscriptions from a confiding and credulous public. And then comes the last act. Secretly, and therefore dishonestly, they put into their own pockets the difference between the real and the pretended price. After a brief career the company is ordered to be wound up. In the course of the liquidation the trick is discovered. Mr. Gluckstein is called upon to make good a portion of the sum which he and his associates had misappropriated. Why Mr. Gluckstein alone was selected for attack I do not know any more than I know why he was only asked to pay back a fraction of the money improperly withdrawn from the coffers of the company.

However that may be, Mr. Gluckstein defends his conduct, or, rather I should say, resists the demand, on four grounds, which have been gravely argued at the bar. In the first place, he says that he was not in a fiduciary position towards Olympia, Limited, before the company was formed. Well, for some purposes he was not. For others he was. A good deal might be said on the point. But to my mind the point is immaterial, for it is not necessary to go back beyond the formation of the company.

In the second place, he says, that if he was in a fiduciary position he did in fact make a proper disclosure. With all deference to the learned counsel for the appellant, that seems to me to be absurd. "Disclosure" is not the most appropriate word to use when a person who plays many parts announces to himself in one character what he has done and is doing in another. To talk of disclosure to the thing called the company, when as yet there were no shareholders, is a mere farce. To the intended shareholders there was no disclosure at all. On them was practiced an elaborate system of deception. * * *

LORD ROBERTSON.—My Lords, I am satisfied of the liability of the appellant. Once the facts are analyzed (and this has been done thoroughly in the Court of Appeal) they are seen to be of no ambiguous import. The appearance of complexity which the case presents arises from the matters in hand having been dressed up artificially, so that things have been separated in language and treatment which in their nature are inseparable and correlative.

To my thinking, the central fact in the history is, that while the object of the syndicate was to make profit out of the resale of Olympia, it was an essential part of the enterprise, as originally designed and as actually carried out, that the same individuals who sold as syndicate should buy as directors. This was provided by the third

head of the agreement which set up the syndicate, and it has a far-reaching effect at all the stages of the argument.

First of all, it seems to me to conclude the question whether these gentlemen were promoters when they bought the mortgages. I do not lay out of account the refreshment contract and the advertising contract, for the entering into contracts for the company is a clear assumption of agency and, therefore, of a fiduciary relation to it. But apart from those contracts, where speculators have formed, exclusively of themselves, the directorate of a company, to be immediately floated for the purpose of buying the property which those same individuals are associated to acquire and resell, they have brought themselves directly within Lord Cairns's statement of the law in *Erlanger's Case*, 3 App. Cas. 1218. They have taken a decisive step in shaping and limiting the company. It may well be asked, if this be not an act of promotion what is? The hypothesis of all the law which we are considering is that the company is not yet formed; and unless these gentlemen had registered the company (and thus passed out of this stage altogether) it is difficult to see what more overt acts of promoting and forming the company they could have done.

The only available argument against this conclusion was that the gentlemen forming the syndicate might have changed their minds and sold to an individual. This is true, but true only in the sense that, till registration of the company and a bargain with the company, they were free to change their minds—true in the sense in which every enterprise not actually consummated may be abandoned. But as matter of fact, these men intended, when they bought the mortgages, to sell to a company constituted in the mode and form described; and they did sell to that company. The appellant in his evidence avows it; and the other facts are indicative, to the point of conclusiveness, that nothing but a company would have served the ends of the syndicate. The mere expression in a deed of the truism that the adventurers could sell to an individual if they did not sell to a company can never avail against the ascertainment of the true facts of the scheme.

The facts here are that the company had been so far organized that its executive was provisionally appointed. The directors of a company are its executive organ; to them its interests are confided; and in the present instance the company, even in this, its inchoate stage, was identifiable through its executive. I hold that from the moment this step was taken the coming directors stood in a fiduciary relation to the company whose interests were to be in their sole hands. This conclusion rests not on technical rules of law, but on the dictates of fair play embodied in law. The people for whom these gentlemen were bound to act were their coming constituents, the persons out of whose money they proposed to make their gain.

And now I pass to the next stage of the case. Assuming the

members of the syndicate to have been promoters at the date of the purchase of the mortgages, did they properly disclose it? In the skilful argument for the appellant the duty of disclosure on this hypothesis was conceded. But this concession must not disarm the criticism which, in considering the adequacy of the disclosure, first ascertains the relevancy of the transaction to the question what sum ought to be paid by the directors for the mortgaged property.

The theory of the appellant is that the purchase of the mortgages was a collateral and independent transaction. It seems to me, on the contrary, to be an essential and inseparable part of one and the same transaction, and for this plain reason that the syndicate's gain on the mortgages had to be paid by the company. The relevancy of the mortgage transaction to the question solved by the syndicate sitting as directors is this—a company, or any one else, considering what price shall be paid draws inferences as to the true value from the price paid by the seller and the proposed advance on that price. In short, what the possible buyer wants to know is the profit to be made by his seller. He may be entitled to know this, or he may not, according as his seller is bound or is not bound to disclose it, but the materiality of the knowledge is indisputable. Again, this transaction had another importance. The inference of value drawn from a competitive sale by auction is founded on the assumption that the sum paid was the least that the property could have been got for. In the present case, that inference would have been unsound. I do not know whether it was necessary, in order to secure the property, that the syndicate in their last bid should advance by 8,000l., whereas all previous advances had been only of 1,000l. But I do know that the appellant had no interest to bid 133,000l. rather than 140,000l., for by the time the biddings had run thus high it was certain that the mortgages would be paid in full, and, as the syndicate knew that the directors would pay their price, it was indifferent to them, to the matter of a few thousands, whether the price which they nominally, and the shareholders really, paid to the vendor was more or less.

On these grounds I consider that the transaction in mortgages was so relevant to the question what price should the company pay for the property that it was necessary that it should be disclosed to the company completely and in detail, and the question is whether this was done. There are several overwhelming reasons for a negative answer.

In the normal case, where the directors are truly and not merely in name the executive of the company, it may be assumed that they will be vigilant and critical of the particulars of a bargain of such paramount importance as the purchase of the property to be traded with, and that, dealing at arm's length, they will examine into anything bearing on that matter that does not tell its own story in its face. But, in the present case, the company was paralyzed so far as vigilance and criticism were concerned; for the board-

room was occupied by the enemy. Now, the question whether adequate disclosure has been made to a company by a vendor bound to do so must necessarily depend upon the intelligence brought to bear on the information. And if, by his own act, the promoter has weakened, or, as here, has annulled the directorate, his case on disclosure becomes extremely arduous—for he has to make out such disclosure to shareholders as makes directors unnecessary. How this could be done we have no occasion to consider, for the appellant is not within sight of doing it. Indeed, the case is so clear that I do not think it is a case of inadequate disclosure, but of direct misrepresentation. Two statements were made which are clearly of that character. The one is the assertion that the purchase of the mortgages was a temporary investment. If this means anything, it means that the syndicate having money on hand awaiting investment in one thing had temporarily put it to another. The contrary is the fact: part of the price of the mortgages was subscribed by the syndicate for its purposes of which this was, in terms, one; and much the greater part was borrowed from their bankers *ad hoc*. The second overt misrepresentation is that the syndicate had paid 140,000*l.* for the property, whereas the truth is that they were paying only 119,265*l.* 13*s.* 11*d.*, the excuse for the former sum having been stated coming to no more than this—that they had to pay the vendor before their own accounts were closed.

I have only to add that I consider the liability of the appellant for the whole sum in the order appealed against to be the necessary result of the ground of judgment which I adopt.

*Order appealed from affirmed and appeal dismissed with costs.**

HEBGEN v. KOEFFLER.

1897. 97 Wis. 313, 72 N. W. 745.⁵

Appeal from a judgment of the circuit court for Milwaukee county.

This was a suit by stockholders on behalf of the corporation and other stockholders to rescind a sale of realty on the ground of fraud and to recover of the promoters of the corporation certain alleged fraudulent profits. The trial resulted in findings in favor of plaintiffs.

MARSHALL, J.—There is no controversy but that the judgment appealed from is sustained by the findings of fact and conclusions of law. Questions of law are discussed in the briefs of counsel

* See also opinion of Lindley, M. R. in the court below, *In re Olympia, Ltd.*, L. R. (1898) 2 Ch. Div. 153, 67 L. J. Ch. (N. S.) 433.

Cf. *In re Cape Breton Co.* (1885) 29 Ch. Div. 795.—Eds.

* Statement abridged and rewritten.—Eds.

but not reached in the consideration of the case, unless some of the findings of fact, to which reference will be made, are first disturbed. The findings, as they stand, are to the effect that defendant Hugo Koeffler, at an expense of \$6,000, obtained the right to purchase of Van Eimeren a tract of land for \$31,000, payable \$600 down, \$13,400 January 2, 1893, and the balance January 2, 1898, with interest; that he then associated with him defendant Preusser in a scheme to form a corporation to take the land for \$55,000 and to divide the profits of the transaction between himself and Preusser, two-thirds to the former and one-third to the latter; that pursuant to such scheme they prepared a subscription paper so worded as not to disclose the true ownership of the land, but to induce signers to believe that it belonged to Van Eimeren, and to bind them to join in forming a corporation to purchase such land for \$55,000, payable \$25,000 down, \$13,000 January 2, 1895, and \$17,000 January 2, 1898, with annual interest; that in order to induce signers not in the scheme to believe that the promoters purposed becoming stockholders on the same basis as others who joined in the apparently mutual enterprise, they each signed for \$10,000 of the stock, and one Fernekes, who was employed to assist in obtaining subscriptions, signed for \$3,000, to make it appear that he was going in with others, while such subscription was in fact for Koeffler; that the whole stock of \$55,000 was subscribed and the corporation was thereupon organized; that Koeffler and Preusser procured themselves to be elected as directors and managing officers, and the sale of the real estate to the corporation to be consummated, ostensibly by Van Eimeren for \$55,000, but really for \$31,000, the promoters taking the difference over the cost to them for profits of the deal, without the other stockholders having any idea but that the purchase was made of Van Eimeren for the full sum of \$55,000.

It needs no discussion of the subject to show that such facts make a clear case for relief against the promoters, either in equity, by or for the benefit of the corporation, to rescind the sale and recover the consideration paid for the property, or in any one of several other ways that might have been adopted. *Pittsburg Mining Co. v. Spooner*, 74 Wis. 307; *Fountain Spring Park Co. v. Roberts*, 92 Wis. 345; *Franey v. Warner*, 96 Wis. 222. The last case cited was very recently decided by this court and the subject there fully discussed and the law stated in substance that, "if a person invites others to join him in the purchase of property at a given price, falsely representing that the purchase is to be made of a third person and that all are to share equally in the cost and equally in the benefits of the enterprise, and such others join with such person on the faith of such representations, and the purchase be made accordingly, each of the bona fide purchasers paying his proportion of the money, and such person acquires secretly a profit to himself by reason of having obtained the property after the making of the

PROMOTERS

mutual agreement at a less sum than it acquires, or by reason of having acquired at a less price, before the sale, it is a fraud. It may, by restoring such person to his original position in the transaction and recover his money in full, or offer to rescind, and, by keeping such person in possession of a rescission of the contract and for a period of time without restoring, he or all similarly situated persons in equity to charge such person as trustee of the property retained by him, and for an accounting of the property retained by him at law for damages for the fraud to the extent of the value he paid by reason thereof. A person who is in a relation of trust and confidence to another person and holds all the profits secretly made by the other person all engaged in the common enterprise, and for the respective interests; and such is the case in this case made by such person before or after the sale of the enterprise."

Appellant, in order to avoid the result of the court and the settled law applicable to the case, the eighteenth finding of fact is contrary to the fact that, if such be not the case, the sale to the corporation is nevertheless ratified by the stockholders who are not contrary to the twenty-seventh finding. The court is to the effect that when the corporation paid for the purchase of the land for \$55,000, it was to make the down payment of \$25,000 by the corporation of the amounts due on the stock subscription, except those in the fraudulent scheme, but the payment to be made of Van Eimeren for the fraud is contrary to the twenty-seventh finding is to the effect that after the time mentioned in the eighteenth finding, the court ratified the conduct of the promoters. The eighteenth finding stands, in view of the other findings, there is no serious controversy, the judgment is unless the twenty-seventh finding be correct, the evidence in the record bearing on each finding is examined with care. No valuable purpose is served by running to it at length or in detail. It is enough to support the findings; hence the judgment is affirmed.

THE TELEGRAPH v. LOETSCHER.

1904. 127 Iowa 383, 101 N. W. 773.*

ACTION in behalf of the Dubuque Specialty Machine Works for money received by Christian Loetscher for promoting the Dubuque Specialty Machine Works, and in aiding another to dispose of property to it. Judgment as prayed, and Loetscher appeals.—Affirmed.

LADD, J.—In April, 1891, A. Ferris Smith was owner of a certain patent right on a mortising machine, and of machinery to manufacture the device. He suggested to citizens of Dubuque the propriety of organizing a company which should purchase these. Thereupon the defendant and two others were appointed by a local board of trade as a committee to go to Chicago, Ill., to examine the mortising machine. Howie and the defendant did so, and seem to have reported that, though not perfect, the invention was valuable. About a week later Smith returned to Dubuque, and, after some parley, induced the defendant, who was superintendent of the Farley & Loetscher Manufacturing Company, to permit him to have the mortising machine set up in its factory for exhibition. He also arranged with Loetscher to help him promote a company for the purchase of the patent and machinery to manufacture the mortising machine. The terms of the agreement are not open to serious doubt, though controverted in argument; the defendant insisting that he was merely to aid in organization of the company, and not in the sale of the patents and machine to it after being organized. The distinction is due to his construction of the contract. The object in organizing the company was that it should acquire the property of Smith, and this was perfectly understood by Loetscher. In a deposition taken in 1896 he testified that Smith proposed that "he would have two hundred shares, or \$20,000, issued to me, if I would help him promote this company. Told him I didn't want any stock, because, if I should get any, I would subscribe for a little myself. Finally told him if he would give me \$10,000 cash, or its equivalent, I would take hold of the matter and help him push it through. He claimed the company should be organized for \$200,000, and he should get 95-200 of the stock and \$50,000 cash for his patent, and he worked along that basis for about a month. Finally Dr. Staples and other prominent men took hold of it, and commenced to deal with Smith. They objected to the amount of cash to be paid to Smith. Smith said to me: 'I'll have to reduce my cash bonus, and I want you to reduce yours.' He said he would take \$25,000 in cash, provided I would be willing to take \$5,000. He made an agreement to pay me \$5,000 cash if the company was organized; otherwise I was not to have anything. I subscribed for the stock myself then, and others subscribed through my influence. That is about the way the company was started."

*Slight portion of opinion omitted.—Eds.

The very purpose of organizing the company was to manufacture the mortising machine and to manufacture the mortising machine paper the defendant helped circulate of the company and the franchise are in the United States," etc. Manifestly Loetsch he testified—"Take hold and help him accomplish this, it was not only necessary but to have it purchase the patent and reach its ultimate object, as defendant knew; and as well as to secure subscribers for stock, and to help him to help Smith accomplish. This is the fact that no settlement was made until consummated. Defendant denies that he organized the company, and insists that it was soon as this was done; but this is mere hearsay was said between him and Smith, and many of the conversation had between him and the circumstances surrounding the fact that defendant exhibited the machine at the factory and requested acquaintances to take stock of the machinist and inventor, his neighbors and were unaware that he was in the secret. To the amount of \$75,000 was subscribed. May a preliminary organization was formed by one of the signers of the articles of incorporation, and afterwards as vice-president was present at nearly all the meetings of the company, advised and participated in the purchase of stock from Smith for which \$6,000 was paid for stock issued; and he was also to have a share in the earnings of the company. It is not material whether or not than originally contemplated in his contract. The important facts are that the defendant was a promoter in organizing the corporation, in buying these patents and machinery, and in organizing the company after it was organized, was a partner of Smith, from whom the purchase was made, and compensation for services in such a capacity, and influence the party may exert with the company, often, though not in this instance, amounting to a defence for money. That his engagement with him a promoter, the record leaves no doubt. He is defined to be one who brings about the formation of a company; who brings together persons interested in the enterprise; who aids and sets in motion the machinery which brings about the corporation itself. 2 Cook on Stocks § 100 said to be a business, not a legal, term

single word a number of business operations, familiar to the commercial world, by which a company is generally brought into existence." Bowen, J., in *Whaley Bridge Calico Printing Co. v. Green*, 28 Wkly. Rep. (Q. B. Div. 1880) 351.

That such persons occupy a fiduciary relation toward the corporation they seek to promote is settled by the authorities. See 23 Am. & Eng. Enc. of Law, 234. In *Bosher v. Richmond, etc., Land Co.*, 89 Va. 455 (16 S. E. 360, 37 Am. St. Rep. 879), the court said:

"A promoter is a person who brings about the incorporation and organization of a corporation. He brings together the persons who become interested in the enterprise, aids in procuring subscriptions, and sets in motion the machinery which leads to the formation itself. Every person, acting by whatever name in the forming and establishing of a company at any period prior to the company, is considered, in law, as occupying a fiduciary relation towards the corporation. He is an agent of the corporation, and is subject to the disabilities of such. He is guilty of a breach of trust if he sells property to the corporation, purchased after he began promoting, without informing the company that the property belongs to him, or he may commit a breach of trust by accepting a bonus or commission from a person who sells property to that corporation."

The promoter is in the situation akin to that of agent or trustee of the company, and his dealings with it must be open and fair. Says Morawetz in his work on Corporations, section 546:

"If persons start a company, and induce others to subscribe for shares, for the purpose of selling property to the company when organized, they must faithfully disclose all facts relating to the property which would influence those who form the company in deciding upon the judiciousness of the purchase. If the promoters are guilty of any misrepresentation of facts or suppression of the truth in relation to the character and value of the property, or their personal interest in the proposed sale, the company will be entitled to set aside the transaction, or recover any compensation for any loss which it has suffered."

The principle is not different from that involved when several persons are engaged in a joint enterprise for their mutual benefit. Each has the right to demand and expect from his associates good faith in all that relates to their common interests, and no one will be permitted to take to himself a secret and separate advantage to the prejudice of the others. *Getty v. Devlin*, 54 N. Y. 403. The principle was forcibly expressed by the Lord Chancellor in *Erlanger v. New Sombrero Phosphate Co., L. R.*, 3 App. Cases, 1218:

"They stand, in my opinion, undoubtedly, in a fiduciary position. They have in their hands the creation and molding of the company. They have the power of defining how and when and in what shape and under what supervision it shall start into existence and begin to act as a trading corporation. If they are doing all this in order

that the company may, as soon as it starts into life, become, through its managing directors, the purchasers of the property of themselves (the promoters), it is, in my opinion, incumbent upon the promoters to take care that in forming the company they provide it with an executive (that is to say, with a board of directors) who shall both be aware that the property which they are asked to buy is the property of the promoters, and who shall be competent and impartial judges as to whether the purchase ought or ought not to be made. I do not say that the owner of property may not promote and form a joint-stock company, and then sell his property to it; but I do say that if he does he is bound to take care that he sells it to the company through the medium of a board of directors who can and do exercise an independent and intelligent judgment on the transaction, and who are not left under the belief that the property belongs, not to the promoter, but to some other person."

In *re North Australian Co. (Archer's Case)* L. R. 1892, Ch. Div. vol. 1, page 322, Archer, being requested by the promoter to become a director, agreed to do so on the former's promise that, if he should at any time wish to part with his shares, he would purchase them at the price Archer paid. After acting some time as director, Archer resigned, and the promoter took his shares at the price agreed. At that time the shares had no market value. The liquidators of the company asked that Archer be required to pay in the amount he had received from the promoter, with interest; and it was held that having regard to his position as director of, and therefore agent for, the company, whatever benefit or profit accrued to him under the indemnity constituted by his secret agreement with the promoter belonged to the company, and that the retention by him of the proceeds of the indemnity occasioned a loss to the company, for which he was accountable, with interest. In *Yale Gas Stove Co. v. Wilcox*, 64 Conn. 101 (29 Atl. 303, 25 L. R. A. 90, 42 Am. St. Rep. 159), Foley and Wilcox agreed that the latter should organize a corporation, to which the former should transfer certain patents at twice the price he was ready to take for them and \$5,000 in capital stock, and of this Wilcox should receive one-half. The company was held entitled to recover from Wilcox all he had received. In *Chandler v. Bacon (C. C.)* 30 Fed. 539, Bacon & Cardoc were promoters of the National Color Printing Company, to be formed, and as such negotiated an agreement between the owners of certain patents by which they were to receive two-sixteenths of its capital stock, less 625 shares which were to be given to one Piper. Bacon was to be elected president, and Cardoc secretary. They offered and sold stock to the public at \$7 per share representing that the patents were to be paid for, but without disclosing the secret agreement by which they were to receive two-sixteenths of the stock without consideration. They were held liable to the receiver of the corporation for the value of the stock at the rate for which they disposed of other stock. See note to *Pittsburg Mining Co. v. Spooner*,

17 Am. St. Rep. 161. The authorities are numerous, and our purpose has been to call attention to a few of the leading ones only.

As promoter and director, the relation of defendant to the company was that of agent, and it is elementary that an agent is disqualified from representing his principal in any transaction in which his personal interests are opposed to the interests of the principal. This rule applies in all cases where there is danger that the agent may be induced to use his powers as agent for his own advantage. The character of the interest is immaterial, provided it is substantial. While duplicity on his part may in a proper case prove a just ground for rescission, his principal may ratify the deal, and claim all the advantages, including any bonus or commission paid the agent by the other party. Indeed, the right of recovery in event of finding it a part of appellant's engagement with Smith to aid him in disposing of his property to the company is not seriously questioned. *Affirmed.*¹

OLD DOMINION COPPER, ETC., SMELTING CO. v.
LEWISOHN.

1907. 210 U. S. 206, 28 Sup. Ct. 634, 52 L. ed. 1025.

The facts are stated in the opinion.

MR. JUSTICE HOLMES delivered the opinion of the court.

This is a bill in equity brought by the petitioner to rescind a sale to it of certain mining rights and lands by the defendants' testator, or in the alternative to recover damages for the sale. The bill was demurred to and the demurrer was sustained. 136 Fed. Rep. 915. Then the bill was amended and again demurred to, and again the demurrer was sustained, and the bill was dismissed. This decree was affirmed by the Circuit Court of Appeals. 148 Fed. Rep. 1020,

¹ See *Erlanger v. New Sombrero Phosphate Co.* (1878) L. R. 3 App. Cas. 1218, affg. 5 Ch. Div. 73; *Yale Gas Stove Co. v. Wilcox* (1894) 64 Conn. 101, 29 Atl. 303, 25 L. R. A. 90, 42 Am. St. 159; *Goodwin v. Wilbur* (1902) 104 Ill. App. 45; *Hayward v. Leeson* (1900) 176 Mass. 310, 57 N. E. 656, 49 L. R. A. 725; *South Joplin Land Co. v. Case* (1891) 104 Mo. 572, 16 S. W. 390 (no disclosure of amount paid by promoters); *Dickerman v. Northern Trust Co.* (1899) 176 U. S. 181, esp. 203-205, 20 Sup. Ct. 311, 44 L. ed. 423; *Chandler v. Bacon* (1887) 30 Fed. 538.

Cf. Fred Macey Co. v. Macey (1906) 143 Mich. 138, 106 N. W. 722, 5 L. R. A. (N. S.) 1036n (effect of laches on right of corporation to rescind); *Densmore Oil Co. v. Densmore* (1870) 64 Pa. St. 43.

In *Downey v. Finucane* (1912) 205 N. Y. 251, Bartlett, J., said: "The promoter of a company, whether he be a director or not, who knowingly issues or sanctions the circulation of a false prospectus containing untrue statements of material facts naturally tending to mislead and to induce the public to purchase its stock or other securities is unquestionably responsible to those who are injured thereby. (*Morgan v. Skiddy*, 62 N. Y. 319.) Where there are a

79 C. C. A. 534. The ground of the isohn, the deceased, and one Bigelo petitioner that they might sell certain that they made their sale while they c in contemplation of a large further is closure of their profit, and that such The Supreme Judicial Court of Mass: entitled to recover from Bigelow upx 188 Massachusetts, 315.

The facts alleged are as follows: ' plan was the mining property of the pany of Baltimore, and also the min question, the latter being held by one l self and of the executors of one Simp the stock of the Baltimore company. May and June, 1895, obtained options Keyser for the purchase of the stock a tion. They also formed a syndicate the agreement that the money subscri be used for the purchase and the sal large advance, and that the members subscriptions, should receive in cash c ration the profit made by the sale. Or Simpson's executors for their stock o cash and notes of himself and Lewis paid in the same way.

On July 8, 1895, Bigelow and Lewis poration, the seven members being the next day the stock of the company wa of twenty-five dollars each, officers w tion became duly organized. July 11, p of the officers resigned, and Bigelow a absent members of the syndicate came

number of such promoters all the co-adven the fraud of an agent employed by them to securities without reference to their own m blower v. Crandall, 7 Mo. App. 220; affd., 7 was said that where an associate in such an c and leaves the details to his companions whi mon accounts his ignorance ought not to ave

Speaking of an equivocal prospectus whic by the House of Lords in Aaron's Reefs v. 273, 285) Lord HALSBURY calls the language sion aptly characterizes that in the present c gued, as it is suggested here, that there w which is proved to be false; but the lord c being regarded as the true test and declared taking the whole thing together was there a 264). And see Greenwood v. Leather Shod 1 Ch. Div. 421 where the court discarded "a t

received from the Baltimore company, the stock of which had been bought, as stated, by Bigelow and Lewisohn, to sell substantially all its property for 100,000 shares of the plaintiff company. The offer was accepted, and then Lewisohn offered to sell the real estate now in question, obtained from Keyser for 30,000 shares, to be issued to Bigelow and himself. This also was accepted and possession of all the mining property was delivered the next day. The sales "were consummated" by delivery of deeds, and afterwards, on July 18, to raise working capital, it was voted to offer the remaining 20,000 shares to the public at par, and they were taken by subscribers who did not know of the profit made by Bigelow and Lewisohn and the syndicate. On September 18, the 100,000 and 30,000 shares were issued, and it was voted to issue the 20,000 when paid for. The bill alleges that the property of the Baltimore company was not worth more than \$1,000,000, the sum paid for its stock, and the property here concerned not over \$5,000, as Bigelow and Lewisohn knew. The market value of the petitioner's stock was less than par, so that the price paid was \$2,500,000, it is said, for the Baltimore company's property and \$750,000 for that here concerned. Whether this view of the price paid is correct, it is unnecessary to decide.

Of the stock in the petitioner received by Bigelow and Lewisohn or their Baltimore corporation, 40,000 shares went to the syndicate as profit, and the members had their choice of receiving a like additional number of shares or the repayment of their original subscription. As pretty nearly all took the stock, the syndicate received about 80,000 shares. The remaining 20,000 shares of the stock paid to the Baltimore company, Bigelow and Lewisohn divided, the plaintiff believes, without the knowledge of the syndicate. The 30,000 shares received for the property now in question they also divided. Thus the plans of Bigelow and Lewisohn were carried out.

The argument for the petitioner is that all would admit that the promoters (assuming the English phrase to be well applied) stood in a fiduciary relation to it, if when the transaction took place, there were members who were not informed of the profits made and who did not acquiesce, and that the same obligation of good faith extends down to the time of the later subscriptions, which it was the promoters' plan to obtain. It is an argument that has commanded the assent of at least one court, and is stated at length in the decision. But the courts do not agree. There is no authority binding upon us and in point. The general observations in *Dickerman v. Northern Trust Co.*, 176 U. S. 181, were obiter, and do not dispose of the case. Without spending time upon the many dicta that were quoted to us, we shall endeavor to weigh the considerations on one side and the other afresh.

The difficulty that meets the petitioner at the outset is that it has assented to the transaction with the full knowledge of the facts. It is said, to be sure, that on September 18, when the shares were is-

sued to the sellers, there were already subscribers to the 20,000 shares that the public took. But this does not appear from the bill, unless it should be inferred from the ambiguous statement that on that day it was voted to issue those shares "to persons who had subscribed therefor," upon receiving payment, and that the shares "were thereafter duly issued to said persons," etc. The words "had subscribed" may refer to the time of issue and be equivalent to "should have subscribed" or may refer to an already past event. But that hardly matters. The contract had been made and the property delivered on July 11 and 12, when Bigelow, Lewisohn and some other members of the syndicate held all the outstanding stock, and it is alleged in terms that the sales were consummated before the vote of July 18 to offer the stock to the public had been passed.

At the time of the sale to the plaintiff, then, there was no wrong done to any one. Bigelow, Lewisohn and their syndicate were on both sides of the bargain, and they might issue to themselves as much stock in their corporation as they liked in exchange for their conveyance of their land. *Salomon v. Salomon & Co.* [1897], A. C. 22; *Blum v. Whitney*, 185 N. Y. 232; *Tompkins v. Sperry*, 96 Maryland, 560. If there was a wrong it was when the innocent public subscribed. But what one would expect to find, if a wrong happened then, would not be that the sale became a breach of duty to the corporation nunc pro tunc, but that the invitation to the public without disclosure, when acted upon, became a fraud upon the subscribers from an equitable point of view, accompanied by what they might treat as damage. For it is only by virtue of the innocent subscribers' position and the promoter's invitation that the corporation has any pretense for a standing in court. If the promoters after starting their scheme had sold their stock before any subscriptions were taken, and then the purchasers of their stock with notice had invited the public to come in and it did, we do not see how the company could maintain this suit. If it could not then, we do not see how it can now.

But it is said that from a business point of view the agreement was not made merely to bind the corporation as it then was, with only forty shares issued, but to bind the corporation when it should have a capital of \$3,750,000; and the implication is that practically this was a new and different corporation. Of course, legally speaking, a corporation does not change its identity by adding a cubit to its stature. The nominal capital of the corporation was the same when the contract was made and after the public had subscribed. Therefore what must be meant is, as we have said, that the corporation got a new right from the fact that new men who did not know what it had done had put in their money and had become members. It is assumed in argument that the new members had no ground for a suit in their own names, but it is assumed also that their position changed that of the corporation, and thus that the indirect effect of their acts was greater than the direct; that facts that gave them no claim gave

one to the corporation because of them, notwithstanding its assent. We shall not consider whether the new members had a personal claim of any kind, and therefore we deal with the case without prejudice to that question, and without taking advantage of what we understand the petitioner to concede.⁸

But, if we are to leave technical law on one side and approach the case from what is supposed to be a business point of view, there are new matters to be taken into account. If the corporation recovers, all the stockholders, guilty as well as innocent, get the benefit. It is answered that the corporation is not precluded from recovering for a fraud upon it, because the party committing the fraud is a stockholder. *Old Dominion Copper Mining and Smelting Co. v. Bigelow*, 188 Massachusetts, 315, 327. If there had been innocent members at the time of the sale, the fact that there were also guilty ones would not prevent a recovery, and even might not be a sufficient reason for requiring all the guilty members to be joined as defendants in order to avoid a manifest injustice. *Stockton v. Anderson*, 40 N. J. Eq. 486. The same principle is thought to apply when innocent members are brought in later under a scheme. But it is obvious that this answer falls back upon the technical diversity between the corporation and its members, which the business point of view is supposed to transcend, as it must, in order to avoid the objection that the corporation has assented to the sale with full notice of the facts. It is mainly on this diversity that the answer to the objection of injustice is based in *New Sombrero Phosphate Co. v. Erlanger*, 5 Ch. D. 73, 114, 122.

Let us look at the business aspect alone. The syndicate was a party to the scheme to make a profit out of the corporation. Whether or not there was a subordinate fraud committed by Bigelow and Lewisohn on the agreement with them, as the petitioner believes, is immaterial to the corporation. The issue of the stock was apparent, we presume, on the books, so that it is difficult to suppose that at least some members of the syndicate, representing an adverse interest, did not know what was done. But all the members were engaged in the plan of buying for less and selling to the corporation for more, and were subject to whatever equity the corporation has against Bigelow and the estate of Lewisohn. There was some argument to the contrary, but this seems to us the fair meaning of the bill. Bigelow and Lewisohn, it is true, divided the stock received for the real estate now in question. But that was a matter between them and the syndicate. The real estate was bought from Keyser by the syndicate, along with his stock in the Baltimore company, and was sold by the syndicate to the petitioner along with the Baltimore company's property, as part of the scheme. The syndicate was paid for it, whoever received the stock. And this means that two-fifteenths of the stock of the corporation, the 20,000 shares sold

⁸ See *Mason v. Carrothers* (1909) 105 Maine 392, at pp. 407-8, 74 Atl. 1030, as to the rights of subsequent innocent purchasers.—Eds.

to the public, are to be allowed to use the name of the corporation to assert rights against Lewisohn's estate that will enure to the benefit of thirteen-fifteenths of the stock that are totally without claim. It seems to us that the practical objection is as strong as that arising if we adhere to the law.

Let us take the business point of view for a moment longer. To the lay mind it would make little or no difference whether the 20,000 shares sold to the public were sold on an original subscription to the articles of incorporation or were issued under the scheme to some of the syndicate and sold by them. Yet it is admitted, in accordance with the decisions, that in the latter case the innocent purchasers would have no claim against any one. If we are to seek what is called substantial justice in disregard of even peremptory rules of law, it would seem desirable to get a rule that would cover both of the almost equally possible cases of what is deemed a wrong. It might be said that if the stock really was taken as a preliminary to selling to the public, the subscribers would show a certain confidence in the enterprise and give at least that security for good faith. But the syndicate believed in the enterprise, notwithstanding all the profits that they made it pay. They preferred to take stock at par rather than cash. Moreover, it would have been possible to issue the whole stock in payment for the property purchased, with an understanding as to 20,000 shares.

Of course, it is competent for legislators, but not, we think, for judges, except by a quasi-legislative declaration, to establish that a corporation shall not be bound by its assent in a transaction of this kind, when the parties contemplate an invitation to the public to come in and join as original subscribers for any portion of the shares. It may be said that the corporation cannot be bound until the contemplated adverse interest is represented, or it may be said that promoters cannot strip themselves of the character of trustees until that moment. But it seems to us a strictly legislative determination. It is difficult, without inventing new and qualifying established doctrines, to go behind the fact that the corporation remains one and the same after once it really exists. When, as here, after it really exists, it consents, we at least shall require stronger equities than are shown by this bill to allow it to renew its claim at a later date because its internal constitution has changed.

To sum up: In our opinion, on the one hand, the plaintiff cannot recover without departing from the fundamental conception embodied in the law that created it; the conception that a corporation remains unchanged and unaffected in its identity by changes in its members. *Donnell v. Herring-Hall-Marvin Safe Co.*, 208 U. S. 267, 273; *Salomon v. Salomon & Co.* [1897], A. C. 22, 30. On the other hand, if we should undertake to look through fiction to facts, it appears to us that substantial justice would not be accomplished, but rather a great injustice done, if the corporation were allowed to disregard its previous assent in order to charge a single member

with the whole results of a transaction to which thirteen-fifteenths of its stock were parties, for the benefit of the guilty, if there was guilt in any one, and the innocent alike. We decide only what is necessary. We express no opinion as to whether the defendant properly is called a promoter, or whether the plaintiff has not been guilty of laches, or whether a remedy can be had for a part of a single transaction in the form in which it is sought, or whether there was any personal claim on the part of the innocent subscribers, or as to any other question than that which we have discussed.

The English case chiefly relied upon, *Erlanger v. New Sombrero Phosphate Co.*, 3 App. Cas. 1218, affirming s. c., 5 Ch. D. 73, seems to us far from establishing a different doctrine for that jurisdiction. There, to be sure, a syndicate had made an agreement to sell, at a profit, to a company to be got up by the sellers. But the company, at the first stage, was made up mainly of outsiders, some of them instruments of the sellers, but innocent instruments, and, according to Lord Cairns, the contract was provisional on the shares being taken and the company formed (p. 1239). There never was a moment when the company had assented with knowledge of the facts. The shares, with perhaps one exception, all were taken by subscribers ignorant of the facts, 5 Ch. D. 113, and the contract seems to have reached forward to the moment when they subscribed. As it is put in 2 *Morawetz, Corp.* (2d ed.) § 292, there was really no company till the shares were issued. Here thirteen-fifteenths of the stock had been taken by the syndicate, the corporation was in full life and had assented to the sale with knowledge of the facts before an outsider joined. There most of the syndicate were strangers to the corporation, yet all were joined as defendants (p. 1222). Here the members of the syndicate, although members of the corporation, are not joined, and it is sought to throw the burden of their act upon a single one. *Gluckstein v. Barnes* [1900], A. C. 240, certainly is no stronger for the plaintiff, and in *Yeiser v. United States Board & Paper Co.*, 107 Fed. Rep. 340, another case that was relied upon, the transaction equally was carried through after innocent subscribers had paid for stock.

*Decree affirmed.*⁹

⁹ See also *Attorney General for Canada v. Standard Trust Co.* (1911) A. C. 498.

Contra, *Old Dominion Copper & Smelting Co. v. Bigelow* (1905) 188 Mass. 315, 74 N. E. 653, 108 Am. St. 479, approved and followed (1909) 203 Mass. 159, 89 N. E. 193 (valuable review of authorities); *Pietsch v. Milbrath* (1905) 123 Wis. 647, 101 N. W. 388, 102 N. W. 342, 68 L. R. A. 945, 107 Am. St. 1017.

Cf. *Erlanger v. New Sombrero Phosphate Co.* (1878) L. R. 3 App. Cas. 1218, affg. 5 Ch. Div. 73; *Commonwealth S. S. Co. v. American Shipbuilding Co.* (1912) 197 Fed. 797. See notes, 8 *Columbia Law Rev.* 567, 22 *Harv. Law Rev.* 48.

In *Mason v. Carrothers* (1909) 105 Maine 392, 74 Atl. 1030, *Cornish, J.*, said (pp. 404-5): "The defendants rely upon a line of cases cited as holding that if such transaction is agreed to by all the stockholders existing at the

ROCKFORD ETC. R. CO. v. SAGE.

1872. 65 Ill. 328, 16 Am. Rep. 587.

MR. JUSTICE SHELDON delivered the opinion of the court:

This was an action of assumpsit, by Sage, against the railroad company, to recover for money paid for surveying done before the company was organized or its charter granted, and for services and expenses as director of the company, and for \$1,000 due on an account stated.

A recovery was had for \$1,000, which, under the evidence, must have been upon what was found to be an account stated.

The defendant appeals.

On the trial below, the plaintiff offered in evidence the following:

"Rockford, Rock Island and St. Louis Railroad Company,

"To Ralph Sage, Dr.

"To money expended and services rendered,—\$1,000.

"STERLING, June 3, 1868.

"(Indorsed) Approved by the executive committee.

"WM. PRATT,

"WM. S. THOMAS."

With proof that Pratt and Thomas were members of the executive committee of the company.

The company was organized some time in the year 1865, the charter having been obtained in the winter of 1865. Plaintiff acted as director about two years. After he had ceased to be director, he presented this bill for services and expenses as director, during all the time he was such, and as commissioner to receive subscriptions for stock. Plaintiff testified to having paid \$50 for surveying in the fall of 1864. It was in evidence that while Greene, Irwin & Co. were negotiating for the road, and as it was about to pass into their hands, the directors of the road talked the matter over among themselves, and they agreed to allow themselves (Sage among the rest) \$1,000 each, for services and expenses.

There was evidence tending to show that Sage's claim was talked over in the board of directors as an organized board, and that it was agreed Sage should have \$1,000.

The following was one of the by-laws of the company:

"Article 6. Whenever any bill against the company shall have been certified correct by a majority of the executive committee, it

time, even though they be dummy stockholders, no fraud is committed upon the corporation and the corporation itself cannot rescind. *Blum v. Whitney*, 185 N. Y. 232, 77 N. E. 1159; *Tompkins v. Sperry, Jones & Co.*, 96 Md. 560, 54 Atl. Rep. 254; *Foster v. Seymour*, 23 Fed. Rep. 65; *McCracken v. Robinson*, 57 Fed. Rep. 375; *Old Dominion Copper Mining Co. v. Lewisohn*, 136 Fed. Rep. 915, 148 Fed. Rep. 1020, *affd.* 210 U. S. 206, 52 L. ed. 1025. These cases, however, with the exception of *Old Dominion Copper Mining Co. v. Lewisohn*, do not support the contention."—Eds.

shall be the duty of the president or vice-president to draw an order on the treasurer for the amount thereof, and of the secretary to countersign the same, which order shall constitute a duly authorized voucher against the company, payable by the treasurer from any funds in his hands."

The executive committee consisted of five members. This bill having been approved by only two of them, it was not properly audited by the executive committee in pursuance of the by-law.

In *Am. Cent. R. R. Co. v. Miles*, 52 Ill. 174, this court recognized and adopted the rule that the law does not imply a promise on the part of railway companies to pay their directors as such, and that it should appear that a by-law or a resolution of the board had been adopted to compensate them for services, before a director can recover for them. Neither such by-law nor resolution here appears. Although there is the testimony of one witness that the matter was talked over by the board when in session, and that it was agreed that Sage should have \$1,000, the witness will not be positive about any action or vote of the board. He says it was concluded to have it put in the shape of a bill, and that he, and Thomas, another member of the executive committee, put their names on the bill, in accordance with the wishes of the board. The record book of the meetings and proceedings of the company shows nothing on the subject of the allowance of the claim, and shows no record of any meeting of the board of directors held between the 16th day of April, 1868, and June 4, 1868; and the record of the meeting of June 4, 1868, shows the following:

"On motion, the following resolution was adopted, to wit:

"Resolved, That the account of Ralph Sage, for services rendered as a director of said company prior to the annual election, in October, A. D. 1867, be referred to a committee, consisting of B. C. Coblentz, James Galt and James E. Abbott."

We find nothing in the evidence which should be considered as amounting to the adoption of any resolution by the board of directors to pay for these services and expenses, or to pay the bill offered in evidence.

There was some evidence tending to show services rendered and expenses incurred by the plaintiff, since the organization of the company, apart from his duty as a director; for all such, he may recover upon a quantum meruit. But there is no proof of such services and expenses to the amount of \$1,000.

For services and expenses before the organization of the company, which, subsequently, the company accepts and receives the benefit of, and promises to pay for, we will not say a party might not recover, in virtue of such express promise; but we are disposed to deny the right of recovery for such services and expenses upon any implied promise resulting from the facts, although the case, cited by appellee's counsel, of *Low v. Conn. Passumpsic River R. R. Co.*, 46 N. H. 284, seems to sanction such a right of recovery; as does also

the case of *Hall v. Verm. and Mass. R.* respects services rendered subsequent to the prior to perfecting the organization of services prior to the act of incorporation.

A right of recovery against a corporation before it had a proper existence, does not satisfy a legal principle.

It appears more reasonable to hold that expenses incurred prior to the organization, if they have been gratuitous, in view of the general expectation that they would result from the object of the corporation to stockholders, who subscribe and pay for their property should be subject to the corporation and which they had no voice in creating.

N. Y. and N. H. R. R. Co. v. Ketchum, 105 N. Y. 105, 49 S. W. 816, 1899. Authority which denies the liability of a corporation for services rendered prior to the perfecting of the corporation, accept the authority of that case as, in the more just and satisfactory rule.

In the language of that case, "it is the duty of the stockholders to see that the corporation are duly organized according to their charter, and impartial directors to conduct their business in effect are *Franklin Fire Ins. Co. v. Hart*, 105 N. Y. 309, 49 S. W. 309, ante, p. 309.

The judgment must be reversed and the judgment reversed.¹⁰

FARMERS' BANK OF VINE

1899. 105 Ky. 816, 49 S. W. 8

JUDGE WHITE delivered the opinion of the court. The appellee by this action sought to recover \$500 for services rendered in organizing the corporation, soliciting stock, superintending the work of the corporation, and various services.

¹⁰ *N. Y. & C. R. Co. v. Ketchum* (1858) 27 Cal. 451; *Cousley* (1874) 72 Ill. 531; *Gent v. Man* 107 Ill. 652; *Hinkley v. Sac & C. Line Co.* (1905) 119 Am. St. 564; *Marchand v. Loan & Pledge Co.* (semble); *Jones v. Smith* (1905) (Tex. Civ. App. 105) 105; *Hall v. Vermont & C. R. Co.* (1856) 28 Vt. 105.

But see *Streator & C. Tel. Co. v. Continental* 577, 75 N. E. 546 (telephone company liable for expenses incurred by promoters and retained); *Wintner v. I. App. Div. (N. Y.)* 30, 91 N. Y. S. 452 (attorney's fees).

In *Gent v. Manufacturers & C. Ins. Co.*, supra.

the date it commenced business. The answer is a denial of any contract, either expressed or implied, or any liability to pay, a denial of the value, and an allegation that the services were rendered gratuitously by appellee. The case was tried before a jury, and resulted in a verdict and judgment for appellee in the sum of \$350. After reasons and motion for new trial had been overruled, this appeal is prosecuted. * * *

From the proof introduced as to the amount and value of the services rendered, there can scarcely be a question as to the amount found by the jury, if, as a matter of law, appellee has shown himself entitled to recover any sum. Appellee actively, and almost exclusively, secured all the stock to be taken. He made trips to Hodgenville, Louisville and Frankfort in the interest of the corporation, superintended the construction of the banking house, let out contracts, negotiated the purchase of the lot on which was erected the banking house, drew the articles of incorporation, and, after the bank began work, gave its officers such advice as they sought. The verdict of \$350 is not unreasonable.

The question of gratuity was submitted to the jury on conflicting evidence, and it cannot be said their verdict is flagrantly against the evidence; and, unless it be so, it will not be disturbed. It is earnestly contended that appellee cannot recover any sum for this service, although it was rendered, and was beneficial and accepted by the appellant, for the reason that he had no contract, and because there was no corporation to make a contract with, and any agreement made by any person before the organization would not bind the corporation, for the reason that it was *ultra vires* as to the corporation. We do not assent to this doctrine. We are of opinion that a corporation is, by an implied contract, liable for such or any services rendered for the use of the corporation as are necessary to its formation, or may be necessary to be done by it, after its incorporation, in furtherance of its corporate business.

The case of *Low v. Railroad Co.*, 54 N. H. 370, is directly in point, and has been approved by this court. It says (page 377): "It may then be safely assumed that under the laws of Vermont the corporation is liable in some form for services necessary to perfect its organization, and which, when such organization was perfected, it accepted, and enjoyed the benefits arising therefrom. Such would be the case in respect to services in obtaining subscriptions to the

corporation should have a full and complete organization and existence as an entity before it can enter into any kind of a contract or transact any business, would seem to be self evident. This is unconditionally true, unless the act of incorporation authorizes the corporators to perform acts and enter into contracts to bind the company when it shall be organized. As well say a child *in ventre sa mere* may enter into a contract, or that its parents may bind it by contract. A corporation, until organized, has no being, franchises or faculties. Nor do those engaged in bringing it into being have any power to bind it by contract, unless so authorized by the charter."—Eds.

capital stock, rendered by a corporate description were, after the organization of course, to entitle the plaintiff to recover. It had been necessary and reasonable, and was in accordance with the understanding and expectation of the plaintiff. This case, *supra*, was expressly so held by the Court of Pennsylvania (Railroad Co. v. Pennsylvania, 101 Pa. 1, 39 Am. R., 39), the court holding: "It is not necessary that a number of persons not incorporated should be brought together in the pursuit of a common purpose, but to procure a charter in the furtherance of which certain acts to be done by one or more persons, with the understanding that compensation shall be made to them when fully formed. And if such persons, with the organization and its objects, and are so organized as to form a company, and the benefit thereof enjoyed by them, such benefits *cum onere*, and make compensation, this principle was recognized in the case of *Co. v. Davis-Rankin Bldg. & Mfg. Co.* [45 S. W. 895], as well as *Morton v. City of St. Louis* [45 S. W. 1]."

It seems to us that any other rule would be to require to organize any corporation, however necessary, to pay for the services, or pay another to do so, howsoever necessary to the organization, if there was no obligation to do so when it is brought into existence. We are of the opinion that the plaintiff is entitled to recover for the services rendered by the defendant, necessary to the organization of the corporation.

We are referred to the case of *Oldham v. City of St. Louis* [45 S. W. 779], decided May 3, 1898. In that case, the corporation cannot be made liable by the representatives of the promoters. The question in that case was whether the stock to defeat the collection of his unpaid stock, on the ground of reason of false and fraudulent representation of the condition and prospects of the corporation, the corporation is not bound by such representation. The stockholder cannot be relieved by reason that the corporation was but dictum. This case is clearly distinguished from the *Oldham* case, *supra*. The charges here are for the organization of the corporation.

Appellant complains of the ruling of the court on the testimony of Young. The effect of the ruling was that a stockholder and a preliminary to the organization, with no knowledge or information of any corporation, was not liable to the appellee for his services, but that the witness was paid, as that was customary in organizations of the kind.

We do not think that the admission of the witness, if any, as alone would authorize a reversal of the judgment.

the jury clearly state the law of the case, and are approved. Finding no error, the judgment is *affirmed*, with damages.¹¹

TUTTLE v. GEORGE A. TUTTLE CO.

1906. 101 Maine 287, 64 Atl. 496.¹²

PEABODY, J.—Assumpsit on promissory note. The case is before the court on motion of defendants for new trial. The action is on a joint promissory note of the defendants to Mary H. D. Tuttle for \$3,000, dated February 11, 1902, with interest at 6 per cent., payable on demand. The jury found a verdict for the plaintiff for the full amount of the note and interest.

The plaintiff is the wife of Edward P. Tuttle. The defendant, John S. Millin, is treasurer of the George A. Tuttle Company and owner of the majority of the capital stock. The defendant, Walter E. Tuttle, is the executor of the will of George A. Tuttle, deceased. George A. Tuttle, an elder brother of Edward P. Tuttle, carried on a dry goods business in Bath. On account of poor health he was obliged to give up his business, and on the eighth of February, 1902, the defendant corporation was organized and George A. Tuttle transferred to said corporation all the merchandise and assets of George A. Tuttle & Co., for which stock was issued in part payment.

The plaintiff claimed that the note was founded upon the following considerations: First, the balance due on a promissory note of the said George A. Tuttle & Co. to the plaintiff assumed by the corporation as one of the obligations of the business purchased by it in accordance with the vote of the directors which authorized the assumption of all outstanding liabilities of the business formerly conducted by George A. Tuttle; second, the services of the plaintiff and her husband in raising three thousand dollars and lending it to the defendant company and the endorsing by Edward P. Tuttle of a promissory note for two thousand seven hundred dollars made by George A. Tuttle to W. W. Pendexter, dated February 8, 1902, pay-

¹¹ Grand River Bridge Co. v. Rollins (1889) 13 Colo. 4, 21 Pac. 897; Morton v. Hamilton College (1896) 100 Ky. 281, 38 S. W. 1, 18 Ky. L. 765, 35 L. R. A. 275, *Accord*.

Cf. Low v. Connecticut &c. R. R. (1864) 45 N. H. 370; Weatherford &c. R. Co. v. Granger (1894) 86 Tex. 350, 24 S. W. 795, 40 Am. St. 837 (able discussion of authorities) and comment, Elliott on Priv. Corps. (4th ed.) sec. 61; In re Empress Eng. Co. (1880) L. R. 16 Ch. Div. 125 (dismissal of claim on contract without prejudice to a claim on quantum meruit); In re English &c. Produce Co., (1906) 2 Ch. Div. 435 ("The idea that a company merely because it has obtained the advantage of the solicitor's work done before the formation of the company is liable in equity for the cost of that work appears to me to be wholly untenable. In my opinion there is no such equity, and any claim based upon it ought to fail," *per* Romer, L. J.).—Eds.

¹² Statement omitted. The case is stated in the opinion.—Eds.

able sixty days after date, whereby they buy out and unite the business of W. Tuttle & Co.; third, the services of E. P. Tuttle buying out W. W. Pendexter, effecting incorporation, and thereafter supervising and managing the same.

The defendants claimed that there was no liability on the note beyond the amount of one hundred dollars, the balance remaining due to George A. Tuttle & Co. In order to find for the whole amount sued for the jury must find facts supporting the second claim, and it is necessary therefore to consider the same and to be rendered as claimed they support the joint promise upon which the note was given, whether the jury were warranted in the evidence introduced.

The plaintiff's second claim can be supported by the testimony of her own and the testimony of Mr. E. P. Tuttle as to the offer made to the promoters of the corporation prior to the execution of the note. It follows: "that if the corporation should give the note we would surrender the note for \$1,400.00 and stand as long as affairs looked all right. If at any time, they to pay the interest on the note, we would pay the question, "What was the \$3,000 note for? securing the business for them, securing the business and advancing \$3,000 cash payment, and for my brother."

It appeared in evidence that both the corporation by Mr. and Mrs. Tuttle and the note and endorsement were afterwards paid, and the \$3,000 note in this suit, so far as it was ever intended to be more than security for the corporation. Mr. and Mrs. Tuttle in temporarily lending the money to the corporation or its promoters. Such is the evidence in this case. Even if it were possible to find that the note was given for a sufficient consideration for a promise to give the note as an additional obligation, such an obligation is inferred from the relations of the parties. E. P. Tuttle himself, who is the actual promoter of the corporation.

The third claim, that of a consideration for the personal services of Mr. E. P. Tuttle, is of no avail. The services in question seem but slight and the circumstance of executing this note and the other reasons of personal interest. If a person is expected or contracted for it does not seem to be the note which is here sued.

But a final defense to the present action is that the note is not a negotiable instrument.

promise by the corporation, one of the parties defendant, beyond the amount of the \$1,400 liability of George A. Tuttle & Co. to the plaintiff.

The following is the record of the directors authorizing the note: "February 8, 1902. Special meeting of the Board of Directors, called by the president, pursuant to the power given him in the by-laws. Present, George A. Tuttle, John S. Millin. It was voted: That the company purchase the stock, fixtures and entire business, including good-will of George A. Tuttle, paying therefor \$2,400 cash and in capital stock of the corporation, 68 shares, and that the company assume all outstanding liabilities of the business formerly conducted by George A. Tuttle and none other. Voted: That the President be directed to give to Mrs. Mary H. D. Tuttle the note of the company for \$3,000, payable on demand, with interest at 6 per cent. per annum, payable every three months, said note being given to cover the outstanding liability of the business of George A. Tuttle."

It appears clearly from the record of the case that whatever rights accrued to the plaintiff or her husband beyond the original \$1,400 were in no sense a liability of the business of George A. Tuttle, but arose from some agreement between E. P. Tuttle and the promoters of the corporation incident to its organization or from benefits conferred on the corporation and accepted by it without contract.

In England it has been held in the more recent cases that in the absence of a charter or statutory provision a contract made by the promoters of a corporation on its behalf before incorporation is a nullity and that the corporation cannot ratify or adopt it and thus make it binding upon it after incorporation, although an action *quasi ex contractu* may be maintained against it if it accepts the benefit of such a contract. *Kelner v. Baxter*, L. R. 2 C. P. 174; *Melhado v. Porto Alegre New Hamburg & B. Ry. Co.*, L. R. 9 C. P. 503; *In re Empress Engineering Co.*, 16 Ch. Div. 125; *In re Northumberland Ave. Hotel Co.*, 33 Ch. Div. 16; 1 *Clark and Marshall*, *Private Corporations*, 306.

A similar view has been taken by the Supreme Court of Massachusetts. *Abbott et als. v. Hapgood et al.*, 150 Mass. 248; *Holyoke Envelope Co. v. U. S. Envelope Co.*, 182 Mass. 171; *Bradford v. Metcalf*, 185 Mass. 205.

A more liberal view is taken by the courts in other states, which hold generally that a contract made by the promoters of a corporation on its behalf may be ratified or adopted by the corporation when organized and that the corporation is then liable both at law and in equity on the contract itself and not merely for the benefits received. *Stanton v. N. Y., etc., Ry. Co.*, 59 Conn. 272; *Smith v. Parker*, 148 Ind. 127; *Grape Sugar and Vinegar Mfg. Co. v. Small*, 40 Md. 395; *Low v. Railroad*, 45 N. H. 370; *Bell's Gap Ry. Co. v. Christy*, 79 Pa. St. 54; *Buffington v. Bardon et al.*, 80 Wis. 635; *Whitney v. Wyman*, 101 U. S. 392.

The American courts, however, insist in every instance on an express resolution or some other act by the corporation subsequent to organization showing an intent to be bound: *Ireland v. Globe Milling and Reduction Co.*, 20 R. I. 190.

Consequently it is held that a corporation is not liable in the absence of ratification or adoption of a charter or statutory provision imposing liability, for the salary of a superintendent or other person for services performed for it before its organization under a contract made by its promoters, although the contract may have been made on its behalf and with the understanding that it should be bound and although the promoters who made it have become its stockholders and officers. *Western Screw & Mfg. Co. v. Cousley*, 72 Ill. 531; *Little Rock & Ft. Smith R. Co. v. Perry*, 37 Ark. 164; *Carey v. Des Moines Co. Op. Coal & Min. Co.*, 81 Iowa 674; 1 Clark and Marshall, *Private Corporations*, 304.

Nor is it bound by an agreement by its promoters that a person shall be employed by it at a certain salary when it shall be organized.

In the case of *Oakes v. The Cattaraugus Water Co.*, 143 N. Y. 430, it was held by a divided court that while such a contract was not binding upon the corporation at its inception, yet it might be ratified by the president on behalf of the corporation when it attained a legal existence, and that there being evidence that the services were performed at the request of the president, who was also the chief promoter of the corporation, and that he acknowledged the indebtedness and promised to pay it, there were, under the circumstances, questions of fact for the jury.

There has not been in the case at bar any resolution or other act of the corporation or of its officers which recognizes a liability on its part to E. P. Tuttle or his wife on account of any agreement made with them by its incorporators. The act of the corporation as evidenced by the vote of the Board of Directors is no such recognition of liability as would amount either to the creation of a new contract by the corporation or the ratification or adoption of a contract originating with the promoters; for by this resolution the note is ostensibly given for another purpose, to pay a liability of the business which it is purchasing. Whatever else may have been the secret intention of the directors individually they were unable to give effect to it by concealing the character of the transaction, and if there was a bona fide claim the plaintiff should have seen to it that the liability of the corporation was definitely established.

Since at the date of the note there was no such liability on the part of the corporation beyond the \$1,400 debt of George A. Tuttle & Co. to the plaintiff which it assumed in part payment of the business, there was a partial failure of consideration, and it was an error to assess the damages at the full amount of the note. The rule is stated in a recent case, "Whenever a promissory note is given for two or more independent considerations and there is a failure of consideration as to one, as where the title to one of the articles sold is not in

the vendor at the time of the sale or where there is a breach of warranty or a misrepresentation as to quality, for the purpose of avoiding circuity of action, the law will allow the defendant in an action between the original parties, or between others standing in no better position, to show such partial failure of consideration in reduction of damages." *Hathorn v. Wheelwright*, 99 Maine 351.

*Motion sustained.*¹³

IN RE LICENSED &c. TRADING ASSN.

1889. L. R. 42 Ch. Div. 1.¹⁴

AFTER a company called the Licensed Victuallers' Mutual Trading Association, Limited, had been formed, but before its shares had been fully offered to the public, George Rudall, an agent of the company, applied on its behalf to Claude Audain, a stock broker and financial agent, who traded as Holloway & Co., to "underwrite" a portion of its shares, which were of the nominal value of £1 each, and an agreement was entered into between them, which was embodied in two letters dated the 19th of March, 1888.

The first of these letters was written to Holloway & Co. by George Rudall, and was as follows:

"Gentlemen,—In consideration of your underwriting £10,000 'A' shares in the Licensed Victuallers' Mutual Trading Association, Limited, at 15 per cent. discount, I, acting on behalf of the company, undertake that all applications which have been received up to the present time, or may be received within one week of the closing of the lists, shall be allotted in full from the said 10,000 shares underwritten by you.

"Yours truly,

"GEO. RUDALL."

¹³ In *Natal Land &c. Co. v. Pauline &c. Syndicate* (1904) A. C. 120, held that a company cannot by adoption or ratification obtain the benefit of a contract purporting to have been made by promoters on its behalf before the company came into existence, and in order to do so, a new contract must be made with it after its incorporation on the terms of the old contract, approving *Kelner v. Baxter* (1866) L. R. 2 C. P. 174. And so, *Pennell v. Lothrop* (1906) 191 Mass. 357, 77 N. E. 842. Cf. *Oakes v. Cattaraugus Water Co.* (1894) 143 N. Y. 430, 38 N. E. 461, 26 L. R. A. 544.

¹⁴ Although the acts of a corporation with reference to the contracts made by promoters in its behalf before its organization are frequently loosely termed "ratification," yet a "ratification," properly so called, implies an existing person, on whose behalf the contract might have been made at the time. There cannot, in law, be a ratification of a contract which could not have been made binding on the ratifier at the time it was made, because the ratifier was not then in existence. In *re Empress Engineering Co.*, 16 Ch. Div. 128; *Melhado v. Porto Alegre, N. H. & B. Ry. Co.*, L. R. 9 C. P. 505; *Kelner v. Baxter*, L. R. 2 C. P. 185. What is called "adoption," in such cases, is, in legal effect, the making of a contract of the date of the adoption, and not as of some former date." *Per Mitchell, J.* in *McArthur v. Times Printing Co.* (1892) 48 Minn. 319, 51 N. W. 216, 31 Am. St. 653.—Eds.

¹⁵ Concurring opinion of Bowen, L. J., omitted.—Eds.

The second letter was written to C
was as follows :—

“Dear Sir,—Referring to your favor
we inclose, we hereby agree to under
Licensed Victuallers’ Mutual Trading
terms named therein.

“P. S.—We further agree to pay the
balance of shares required to make up
date.

On the 14th of April, 1888, the com
and 8555 shares were in pursuance of
and without any further application
to Claude Audain under the name of
such allotment was given to him on the

On the 17th of April, Claude Audain
notice of allotment which had been sent
wrote to the secretary declining to take

On the 23rd of May a resolution
winding-up of the company, and on
made that the voluntary winding-up
supervision of the court.

On the 17th of August, 1888, the
Holloway & Co. on the list of contrib
shares.

Claude Audain then applied to be
tributories, and his motion for that
Justice Chitty on the 20th of December

Mr. Justice Chitty considered that
ter of the 19th of March, 1888) must
so many of the 10,000 shares to which
extended as might not be applied for
and that whatever question might have
case was merely the common case stated
the Companies Act, 1867. The parties
parently not aware of the fact that issue
per cent. was beyond the powers of the
the application not having been made
must be refused with costs.

From this decision Claude Audain
COTTON, L. J.—

This is an appeal from the refusal
relieve the appellant from liability in
which had been allotted to him in
up, as the balance required to make
shares. The substantial question is whether

under any liability at all in respect of the shares so allotted to him. That question turns upon the contract, and the contract, if any, is to be found in the underwriting agreement which was entered into between the appellant and an agent of the Licensed Victuallers' Mutual Trading Association. From the evidence which has been given as to the meaning of the expression "underwriting" as applied to shares, it appears that an "underwriting" agreement means an agreement entered into before the shares are brought before the public, that in the event of the public not taking up the whole of them, or the number mentioned in the agreement, the underwriter will, for an agreed commission, take an allotment of such part of the shares as the public has not applied for. That is what is meant when it is said that a person has agreed to underwrite a certain number of shares in a company, and that is in my opinion what was meant by the term "underwrite" in the present agreement. "Underwriting" is a well-known thing in connection with the formation of companies. The appellant in agreeing to "underwrite" a certain number of shares has agreed to do this particular thing, and in my opinion he is just as much bound in equity as if the thing which he was to do had been set out at length in the contract which was entered into. [His Lordship then read the letters of 19th of March, 1888, and continued:] It appears to be the usual course that some formal application should be made for the shares, and it is said that there should have been some formal application made for allotment of the shares in the present case. But the postscript to the letter written by the appellant shews that he considered that what he had done amounted to an application, and that he himself treated the letter not only as a guarantee, but as an application for allotment, and in my opinion it must be regarded as an application to take the balance of the shares required to make up the £10,000.

A further question arises as to the meaning of the expression underwriting "at 15 per cent. discount." It appears from the evidence that the expression "discount" is an unusual term in connection with the underwriting of shares, and that it is not a term to which any meaning of art can be given; and it further appears that under an underwriting agreement a commission is paid on all the shares to which the agreement applies, whether taken by the public or by the underwriter himself. But the court must put a construction on the word. And I think that upon the fair construction of the words used, they mean not "discount" in the proper sense of the term, but merely "commission," the amount to be paid to the underwriter in respect of the shares which he underwrote. It is not really a sum to be deducted from the nominal amount of the shares when they are applied for and allotted, but a sum to be paid on all the shares underwritten. That being so, it was not an agreement to allot shares at 15 per cent. discount, but to pay 15 per cent. commission to the appellant in consideration of his having made the contract with the company. I think therefore that the decision of Mr. Justice Chitty

was right in not removing the appellant's respect of these shares. The appeal must be dismissed with costs.

LINDLEY, L. J.—

I am of the same opinion. The case is of great importance to persons engaged in public subscription. I doubt the court had upon it was with the meaning of "underwriting," of which, as applied to the exact meaning. We did not know the meaning in the line of business to which they have now had the advantage of the persons who are accustomed to this kind of business. Their evidence is, I think, clear enough to mean "place," the meaning of which explains *Gorrissen's Case*, Law Rep. 8 Ch. 507. "Underwriting," in this kind of business, means many shares, more or less in number, as shown by the writing letter if the public do not subscribe. I doubt now that that is the meaning of "underwriting."

Then a question arises as to what was meant by "15 per cent. discount." That is an amount which means that the shares to be taken by the public are to him at a discount, that is to say, that it has the effect that those shares are fully paid for at 15 per cent. Upon the other hand, it may mean that it may have no definite meaning at all. It can be construed as using the word "discount" in two senses. I do not see that there is anything to bind the company, if it could be bound, to do that which was wholly *ultra vires* that in consideration of receiving 15 per cent. to underwrite so many shares. That makes the transaction consistent and businesslike, and in accordance with the intentions of the parties. The postscript throws this light upon the matter or removes any suggestion that there was any application for shares. It is an agreement between the appellant and the respondent which says: "We further agree to pay for the shares." There is here a clear agreement that so many as the public do not subscribe, the secretary to issue an allotment. Consequently he is rightly placed upon the appeal must be *dismissed with costs*.¹⁵

¹⁵ See *Carmichael's Case* (1896) 2 Ch. Div. 1 (attorney to promoter or vendor irrevocable); *Re &c. Mines* (1897) 1 Ch. Div. 575 (underwriting acceptance); *Barrow v. Paranga Mines* (1909) 100 Q.B. 1; *Prince v. Prince* (1907) 195 Mass. 242, 81 F. 2d 1; *Harrison* (1905) 140 Fed. 519; *Warburton v. Harrison* 86 C. C. A. 173.—Eds.

CHAPTER XI.

DISSOLUTION.

Co. Lit. 13b. And it is to be well observed that our author saith, *if he hath no heire, &c. the land shall escheate*. In which words is implied a diversity (as to the escheate) between fee simple absolute, which a natural body hath, and fee simple absolute, which a body politique or incorporate hath. For if land holden of *I. S.* be given to an abbot and his successors, in this case if the abbot and all the convent die, so that the body politique is dissolved, the donor shall have again this land, and not the lord by escheat. And so if land be given in fee simple to a deane and chapter, or to a mayor and commonalty, and to their successors, and after such body politique or incorporate is dissolved, the donor shall have again the land, and not the lord by escheate. And the reason and the cause of this diversity is, for that in the case of a body politique or incorporate the fee simple is vested in their politique or incorporate capacity created by the policy of man, and therefore the law doth annex the condition in law to every such gift and grant, that if such body politique or incorporate be dissolved, that the donor or grantor shall re-enter, for that the cause of the gift or grant faileth; but no such condition is annexed to the estate in fee simple vested in any man in his naturall capacity, but in case where the donor or feoffor reserveth to him a tenure, and then the law doth imply a condition in law by way of escheate.¹

1 Bl. Com. 485. A corporation may be dissolved, 1. By act of parliament, which is boundless in its operations. 2. By the natural death of all its members, in case of an aggregate corporation. 3. By surrender of its franchises into the hands of the king, which is a kind of suicide. 4. By forfeiture of its charter, through negligence or abuse of its franchises; in which case the law judges that the body politic has broken the condition upon which it was incorporated, and thereupon the incorporation is void. And the regular course is to bring an information in the nature of a writ of *quo warranto*, to inquire by what warrant the members now exercise their corporate power, having forfeited it by such and such proceedings.

¹ But see *Johnson v. Norway* (1623) Winch. 37; s. c., Co. Lit., Harg., Book I, 13b, note 71. See article by S. Williston, 2 Harv. Law Rev. at pp. 163-5. —Eds.

ence or death of the plaintiff may properly be pleaded in abatement. 1 Chitty's Pl. 482; Story's Pl. 24. But whether, as it entirely and perpetually destroys the plaintiff's right to recover, it may not also be pleaded in bar, it is not necessary to determine. Proprietors of Monumoi v. Rogers, 1 Mass. R. 159; First Parish in Sutton v. Cole, 3 Pick. 245. Whether the plea conclude in abatement or bar, the issue being found against the defendant, the judgment must be peremptory. The established rule is, that in dilatory pleas, when the issue is found against the defendant on matters of fact, the judgment must be in chief. Gould's Pl. 300; Howe's Pract. 215.

The principal question for our consideration is, whether judgment shall be rendered on the verdict. The defendant's counsel contends that the evidence introduced will not support the verdict, but that the verdict is against the evidence and the law and should be set aside.

The point which has been determined by the jury, though necessary to be submitted to them with proper instructions, is quite as much a matter of law as of fact; and we the more readily enter into the examination of it.

The legal establishment and due organization of the corporation were admitted; but it was contended that the facts disclosed showed a dissolution of it.

The elementary treatises on corporations describe four methods in which they may be dissolved. It is said that private corporations may lose their legal existence by the act of the legislature; by the death of all the members; by a forfeiture of their franchises; and by a surrender of their charters; 2 Kyd on Corp. 447; 1 Bl. Comm. 485; 2 Kent's Comm. (1st ed.) 245; Angell & Ames on Corp. 501; Oakes v. Hill, 14 Pick. 442. No other mode of dissolution is anywhere mentioned or alluded to.

1. In England, where the parliament is said to be omnipotent and where in fact there is no constitutional restraint upon their action, but their own discretion and sense of right, corporations are supposed to hold their franchises at the will of the legislature. But if they possess the power to annul charters, it certainly has been rarely exercised by them. In this country, where the legislative power is carefully defined by explicit fundamental laws, by which it must be governed and beyond which it cannot go, it has become a question of some difficulty to determine the precise extent of their authority in relation to the revocation of charters granted by them. But as it is not pretended that there has been any legislative repeal of the plaintiffs' charter, it will not be useful further to discuss this branch of the subject.

2. As all the original stockholders are not deceased, the corporation cannot be dissolved for the want of members to sustain and exercise the corporate powers. Besides, this mode of dissolution cannot apply to pecuniary or business corporations. The shares, being property, pass by assignment, bequest, or descent, and must ever remain

the property of some persons, who of necessity must be members of the corporation as long as it may exist.

3. Although a corporation may forfeit its charter by an abuse or misuser of its powers and franchises, yet this can only take effect upon a judgment of a competent tribunal. 2 Kent's Comm. (1st ed.) 249; *Corporation of Colchester v. Seaber*, 3 Burr. 1866; *Smith's Case*, 4 Mod. 53. Whatever neglect of duty or abuse of power the corporation may have been guilty of, it is perfectly clear that they have not lost their charter by forfeiture. Until a judicial decree to this effect be passed, they will continue their corporate existence. *The King v. Amery*, 2 T. R. 515.

4. Charters are in many respects compacts between the government and the corporators. And as the former cannot deprive the latter of their franchises in violation of the compact, so the latter cannot put an end to the compact without the consent of the former. It is equally obligatory on both parties. The surrender of a charter can only be made by some formal solemn act of the corporation; and will be of no avail until accepted by the government. There must be the same agreement of the parties to dissolve, that there was to form the compact. It is the acceptance which gives efficacy to the surrender. The dissolution of a corporation, it is said, extinguishes all its debts. The power of dissolving itself by its own act, would be a dangerous power, and one which cannot be supposed to exist.

But there is nothing in this case which shows an intention of the corporators to surrender or forfeit their charter, nor anything which can be construed into a surrender or forfeiture.

The possession of property is not essential to the existence of a corporation. 2 Kent's Comm. (1st ed.) 249. Its insolvency, cannot, therefore, extinguish its legal existence. Nor can the assignment of all its property to pay its debts, or for any other purpose, have that effect. The instrument of assignment was not so intended, and cannot be so construed. All its provisions look to the continuance of the corporation. It contains covenants that the assignees may use the corporate name for the collection of the debts and the disposition of the property assigned; that the corporation will not hinder or obstruct them in the performance of these functions; that it will make any further conveyances and assurances which may become necessary, and will do and perform any other and further acts which may be required to enable the assignees fully to execute their trust. The instrument which covenants for future acts, cannot be construed to take away all power of action.

The omission to choose directors clearly does not show a dissolution of the corporation. Although the proper officers may be necessary to enable the body to act, yet they are not essential to its vitality. Even the want of officers and the want of power to elect them, would not be fatal to its existence. It has a potentiality which might, by proper authority, be called into action, without affecting the identity of the corporate body. *Colchester v. Seaber*, 3 Burr. 1870.

But here, in fact, was no lack of officers. Although no directors had been chosen for several years, yet, by the by-laws of the corporations, the directors, though chosen for one year, were to continue in office till others were chosen in their stead.

The damages were properly assessed by the jury. The defendant having elected to try her case upon a plea in abatement, must submit to the legal consequences of that form of trial. Perhaps the Court might have assessed the damages as in case of default. But most obviously the better course was to submit the subject to a jury. In doing this the defendant could not be allowed to go into the whole defence as upon the general issue. The rule adopted at the trial was the correct one.

*Judgment according to verdict.**

SWAN LAND AND CATTLE CO. v. FRANK.

1893. 148 U. S. 603, 37 L. ed. 577, 13 Sup. Ct. 691.*

MR. JUSTICE JACKSON delivered the opinion of the court.

The appeal in this case presents for our consideration and determination the question whether the Circuit Courts of the United States can properly entertain jurisdiction of a suit in equity which unites and seeks to enforce both legal and equitable demands, when the right to the equitable relief sought rests and depends upon the legal claim being first ascertained and established, and where the person against whom such legal demand is asserted is not made a party defendant; or, stated in another form more directly applicable to the present case, can a party having a claim for unliquidated damages against a corporation, which has not been dissolved, but has merely distributed its corporate funds amongst its stockholders, and ceased or suspended business, maintain a suit on the equity side of

* It is generally held that a surrender must be accepted. *Contra*, *Savage v. Walshe* (1855) 26 Ala. 619; *Merchants' & Planters' Line v. Waganer* (1882) 71 Ala. 581. And see *State ex rel. Chilhowee v. Woolen Mills Co.* (1905) 115 Tenn. 266, 89 S. W. 741, 2 L. R. A. (N. S.) 493, 112 Am. St. 825, where a majority of the stockholders voted by formal resolution to surrender the charter; there was no acceptance, but it was held that the surrender was sufficient to justify a suit under a section of the Tennessee code providing for a dissolution by judicial decree in case of the surrender of corporate rights.

As to the effect of the death of all the members, see *State v. Trustees of Vincennes University* (1854) 5 Ind. 77; *McGinty v. Athol Reservoir Co.* (1892) 155 Mass. 183, 29 N. E. 510; *Harris v. Mississippi Valley & C. R. Co.* (1875) 51 Miss. 602, esp. p. 610; *Philips v. Wickham* (1829) 1 Paige Ch. (N. Y.) 590 (loss of an integral part of the corporation); *Lehigh Bridge Co. v. Lehigh Coal & Navigation Co.* (1833) 4 Rawle (19 Pa.) 9 (suspension distinguished from extinction of franchise). See also *Elliott, Priv. Corps.* (4th ed.) sec. 598.—Eds.

* Only portions of the opinion are given. Dissenting opinion of Mr. Justice Brown omitted.—Eds.

the United States Circuit Court against the holders, to reach and subject the assets to payment and satisfaction of his claim, to claim to judgment and without making any payment and bringing it before the court?

* * * * *

The general rule that suits in equity concerning corporations be rendered, when necessary or in suits against corporations or individuals, are not brought in equity, are not affected by section 1 of the act of February 13, 1893, enacted in section 737 of the Revised Statutes. This court has repeatedly held. *Shields v. Coiron et al. v. Millaudon*, 19 How. 111; *Co. v. Co.*, 22 How. 380; *Barney v. Baltimore & Annapolis R. Co.*, 18 Wall. 626. The same rule is applied to suits as to citizenship of necessary parties to suits, and the right of removal. *Thayer v. Life Insurance Co.*, 11 U. S. 717, 719; *St. Louis & San Francisco R. Co. v. U. S.*, 60, 62.

To take the present case out of the operation of the act, it is argued on behalf of appellants that the corporations have a total abandonment of their franchises as to the vendor corporations. We cannot say that the dissolution of corporations is or may be effected by their charters, by failure of any essential elements of organizations that cannot be restored, by the loss of their franchises with the consent of the state, or by the judgment within constitutional authority, by the state and judgment of dissolution declared in a decree of the court or by other lawful means. No such dissolution is shown. The averments that said corporations proceeded to thereafter distributed their remaining assets among the stockholders, and have since made no further business, have no agent or officer upon whom process can be served, assets out of which any judgment against them could be paid, fall far short of a dissolution such as would be effected by the corporations or their trustees as promoters, to establish the validity and amount of the claim for damages. (Secs. 506, 515). The corporation, when the corporation is dissolved, the need for a decree is dispensed with, need not, therefore, be made, but is applicable to the present case.⁴

⁴ *Reichwald v. Commercial Hotel Co.* (1883) 100 N. Y. 401; *Co. v. Sylvester* (1893) 68 Hun (N. Y.) 401, 180; *Parker v. Bethel Hotel Co.* (1896) 96 N. Y. 706; *Weigand v. Alliance Supply Co.* (1896) 96 N. Y. 803. *Accord.* In the first cited case, *Shelden v. Commercial Hotel Co.*, the effect of this transfer of all the hotel property to the stockholders, the business of the corporation; but that was

MATTER OF BROOKLYN, WINFIELD, ETC. R. CO.

1878. 75 N. Y. 335.

APPEAL from order of the General Term of the Supreme Court, in the second judicial department, affirming an order of Special Term which denied a motion for the appointment of commissioners to appraise the compensation to be made to the Brooklyn Railroad Company for the use of its tracks, the right to which was sought to be acquired by the petitioner.

The decision upon a former proceeding is reported in 72 N. Y. 245.

The facts appear sufficiently in the opinion.

ANDREWS, J. This court in the former proceeding taken by the petitioner for the appointment of commissioners of appraisal, affirmed the order of the Special and General Terms, denying the prayer of the petition on the ground that in September, 1877, when the proceeding was instituted, the Brooklyn, Winfield, and Newtown Railroad Company, had ceased to be a corporation, and was extinct by its failure to construct its road within the time limited by chapter 775, of the Laws of 1867, or within the three years for which the time was extended by chapter 575 of the Laws of 1874.

In the former proceeding it was claimed on the part of the petitioner in answer to the objection that the corporation had not commenced the construction of its road within five years from the time of filing the articles of association, or within the extended time given by the act of 1874, that such neglect or omission created simply a cause of forfeiture, of its corporate franchises, and a ground of proceeding by the attorney-general to have the corporation dissolved, and that its existence and powers continued until the forfeiture was judicially ascertained and declared, and that until that time it could exercise any of the franchises conferred upon it by the statutes under which it was incorporated, including the power given by chapter 622 of the Laws of 1871, to acquire the right to use the tracks of the Broadway Railroad Company in certain streets, in the city of Brooklyn, where the routes of the two corporations were coincident.

This court in affirming the order appealed from, recognized the general principle that a corporation by omitting to perform a duty imposed by its charter, or to comply with its provisions, does not ipso facto lose its corporate character, or cease to be a corporation, but simply exposes itself to the hazard of being deprived of its corporate character and franchises by the judgment of the court in an

is entirely clear, upon the authorities, that the disposal of all the property of a corporation has not the effect to end or dissolve the corporation."

But see *Slee v. Bloom* (1821) 5 Johns. Ch. (N. Y.) 366, (1822) 19 Johns. (N. Y.) 456, 10 Am. Dec. 273. Cf. *Moore v. Whitcomb* (1871) 48 Mo. 543; *State Savings Assn. v. Kellogg* (1873) 52 Mo. 583.—Eds.

action instituted for that purpose by the attorney-general in behalf of the people. But while affirming this general proposition the court held that by force of section 47 of the general railroad act of April 2, 1850 (chap. 140), as amended by chapter 775 of the Laws of 1867, which declares that if any corporation formed under the act shall not within five years after its articles of association are filed and recorded in the office of the secretary of state, begin construction of its road, and put it in operation in ten years from the time of filing its articles of association, "its corporate existence and powers shall cease," the corporate existence of the petitioner absolutely terminated, and the corporation became extinct by reason of its failure to commence the construction of its road, within the time limited by the statute of 1867, or the extended time given by the act of 1874, and upon the ground that the petitioner had no corporate existence when the proceeding then under review was taken, the order denying the relief asked was affirmed. The court regarded a corporation organized under the act of 1850, which had not complied with the act of 1867, as extinct by virtue of an express limitation upon the original grant of corporate power, and ALLEN, J., in delivering the opinion of the court, said: "It needed no action or judicial procedure to declare or complete a forfeiture of the charter, and loss of corporate power."

After the decision of the court in that case, the Legislature on May 2, 1878, passed an act (chap. 206), purporting to be an amendment of chap. 575 of the Laws of 1874, as follows: "Section 1. The time within which the Brooklyn, Winfield and Newtown Railway Company is required by law to finish its road, and put it in operation is hereby extended five years, from and after the passage of this act." The present proceeding was commenced in July, 1878, and differs from the former one in no material respect, except that the petitioner sets out in its petition the act of May, 1878, as an authority for the present application.

This act is claimed to be unconstitutional, on the ground that it violates sec. 18, art. 3, of the Constitution, which took effect January 1, 1875, which declares among other things, that "the Legislature shall not pass a private or local bill, * * * granting to any corporation, association, or individual, the right to lay down railroad tracks." I am unable to see any answer to this objection. When the statute in question was passed, the "Brooklyn, Winfield, and Newtown Railway Company," had ceased to be a corporation. Its powers were not simply suspended, or in abeyance, but the corporation itself was extinct. It had not by its failure to commence its road within the time limited, simply incurred a liability to forfeiture, but it had ceased to exist as fully and completely as if judgment of forfeiture had been pronounced against it. This is the necessary conclusion from our former decision. The act of 1878 was not a waiver by the Legislature of a forfeiture incurred by an existing corporation, but it was the creation of a new corporation, under the

guise of reviving and rehabilitating a defunct corporate body. If this legislation can stand the test of the Constitution, then the hundreds of street railway and other charters long since supposed to be dead, may be legislated into life. I think it is impossible to distinguish the power attempted to be exercised by the Legislature by the act in question, from a mere legislative grant of a special charter to construct and operate a street railway, and this is plainly prohibited by the Constitution.

We have decided in the Matter of the N. Y. Elevated R. R. Co. (70 N. Y. 327), that it is competent for the Legislature since the constitutional amendment of 1874, to waive a cause of forfeiture existing against a corporation, and relieve it from the liability incurred by its omission to construct its road within the time prescribed in its charter. But in that case the corporation in respect to which the legislation in question was had, was not subject to the provisions of § 47, of the general railroad law. It was the case of an existing corporation subject to be proceeded against by the attorney-general, but whose franchises and powers had not been extinguished or lost.

The order of the General Term should be affirmed.

All concur.

*Order affirmed.*⁵

STATE EX REL. JOHNSON v. SOUTHERN BUILDING & LOAN ASS'N.

1902. 132 Ala. 50, 31 So. 375.⁶

TYSON, J.—This is an information in the nature of a quo warranto filed under section 3417 et seq. of the Code seeking to forfeit

⁵ Brooklyn Steam Transit Co. v. Brooklyn (1879) 78 N. Y. 524, *Accord*. Wallamet Falls &c. Co. v. Kittredge (1877) 5 Sawy. (U. S.) 44, Fed. Cas. No. 17105, *Contra*.

Cf. Matter of N. Y. Elevated R. Co. (1877) 70 N. Y. 327, 3 Abb. N. C. 401; Matter of Kings County Elevated R. Co. (1887) 105 N. Y. 97, 119-120, 13 N. E. 18 (distinguishing and explaining the principal case); Day v. Ogdensburgh &c. R. Co. (1887) 107 N. Y. 129, 139, 13 N. E. 765; N. Y. &c. Bridge Co. v. Smith (1896) 148 N. Y. 540, 42 N. E. 1088 (holding that where the legislature says that the charter shall be null and void, the meaning is that it shall be null and voidable and an action is necessary.) In the last cited decision, Bartlett, J., said: "It requires, however, strong and unmistakable language * * * to authorize the court to hold that it was the intention of the legislature to dispense with judicial proceedings on the intervention of the attorney-general." (p. 547) But, as was also indicated, "the question as to whether a forfeiture clause is or is not self-executing, depends wholly upon the language employed by the legislature." (p. 547)

See also Owensboro Wagon Co. v. Bliss (1901) 132 Ala. 253, 31 So. 81, 90 Am. St. 907; People v. Rosenstein-Cohn Cigar Co. (1900) 131 Cal. 153, 63 Pac. 163; Belleville v. Citizens' Horse R. Co. (1894) 152 Ill. 171, 38 N. E. 584, 26 L. R. A. 681; Parker v. Bethel Hotel Co. (1895) 96 Tenn. 252, 34 S. W. 209, 31 L. R. A. 706.—Eds.

⁶ Portion of opinion omitted.—Eds.

the charter of the Southern Building & Loan Association, a corporation organized under the general laws of the State. The petition is filed in the name of the State on the relation of Thomas L. Johnson, and by said Johnson in his own behalf. As originally framed it alleged numerous conclusions of law and fact, without separating them into counts or otherwise designating the several causes of action. This was informal. *Highland Ave. & Belt R. R. Co. v. Dusenberry*, 94 Ala. 413; *R. & D. R. R. Co. v. Weems*, 97 Ala. 270. The petition, after demurrer sustained, was twice amended, and as amended, was separated into several counts. We need only consider it as last amended since it contains, in what was conceived to be better form, all that was originally alleged as grounds of complaint, with the exception of the alleged failure to make returns required to be made by building and loan companies to the State auditor by section 1129 of the Code. While this ground need not be separately discussed, since it can be disposed of on general principles applicable to other counts of the petition, yet it may not be amiss to call attention to the fact that section 1130 provides a penalty for the violation complained of.—*State v. Real Estate Bank*, 41 Am. Dec. 109.

As last amended the demurrer was sustained, and the plaintiff declining to amend further, the petition was dismissed. This action of the court is now assigned as error.

* * * * *

But there is another proposition upon which the action of the court in sustaining the demurrers must be affirmed, without reference to the form of the pleadings. While an information in the nature of a quo warranto is generally recognized as the appropriate proceeding of testing the right to exercise corporate functions and as the proper corrective for misuses or non-user or abuse of corporate franchises, it is not for the commission of every act ultra vires that a charter will be declared forfeited. The abuse must be willful, continued and relate to the essence of some franchise granted.—Note on page 180 of 8 Am. St. Rep., where all the cases are collated. See also *State v. Tombeckbee Bank*, 2 Stew. 30. It must also appear that the matter complained of is of such character, that no adequate relief can be obtained in any other mode. Courts are averse to declaring forfeitures, especially at the suit of individuals who show no interest in the matter complained of. The dominant idea in every case where a forfeiture can properly be declared is that the State should resume the franchise granted because of the abuse of it, thus involving a breach of duty to the State. True, wrongs to individuals may be made the predicate of an information of the kind, but they should be of such a character as that they involve, in the sense mentioned, an offense also against the grant of the State. Wrongs done creditors and stockholders in the course of the administration of the company's affairs, by the assumption of questionable rights, should not be made a ground of forfeiture, especially when it appears a remedy exists otherwise. The rights of stockholders are contract

rights, and it cannot be doubted that there is a sufficient remedy in the ordinary processes of the courts for such injuries as are complained of, if they exist in fact.—*Bank v. Francis*, 115 Ala. 324, and cases therein cited. The acts of commission and omission here attempted to be charged do not pertain to the grant in its essence and are not such as justify a forfeiture of the charter. In the case of *Minnesota v. Minn. Thresher Mfg. Co.*, 40 Minn. 213, will be found a very full and able discussion of the controlling principles to which we give our assent. While we do not commit ourselves to the distinction there made between rights acquired under general charters and franchises acquired by special grant, we do concur in the limitations within which such proceedings may be maintained. It is said: "Acts in excess of power may undoubtedly be carried so far as to amount to a misuser of the franchise to be a corporation and a ground for its forfeiture. How far it must go to amount to this the courts have wisely never attempted to define except in very general terms, preferring the safer course of adopting a gradual process of judicial inclusion and exclusion as the cases arise. But we think it may be safely stated as the general consensus of the authorities that to constitute a misuser of the corporate franchise, such as to warrant its forfeiture, the ultra vires acts must be so substantial and continued as to amount to a clear violation of the condition upon which the franchise was granted and so derange or destroy the business of the corporation that it no longer fulfills the end for which it was created." In *High on Extraordinary Remedies* (§ 649), the same principle is thus announced: "It is to be observed that the courts proceed with extreme caution in proceedings which have for their object the forfeiture of corporate franchises, and a forfeiture will not be allowed except upon express limitation, or for a plain abuse of power by which the corporation fails to fulfill the design and purpose of its organization. Especially are the courts inclined to look with disfavor upon such forfeitures when the law has provided other sufficient remedies; and when an adequate legal remedy is provided in damages the corporate franchise will not be forfeited until an entire derangement of the corporate affairs is shown." Authorities might be multiplied holding to the same proposition.—*State v. Real Estate Bank*, supra; *People v. Hillsdale Co.*, 2 Johns. 190, 9 Am. & Eng. Ency. Law (2d ed.), 573, 574, and note 2 on page 574.

It is scarcely necessary, in conclusion, to say that we intimate no opinion upon the propriety or otherwise of the corporate acts attempted to be complained of or as to the forum in which these questions may be tried. It is sufficient for this case, that the remedy does not lie in a forfeiture of the charter.

*Affirmed.*¹

¹ See also *State ex rel. Scott v. U. S. & C. Trust Co.* (1903) 140 Ala. 610, 37 So. 442, 103 Am. St. 60, ("* * * courts are clothed with a discretion which they may exercise, even though there may have been a violation by the corporation of the charter contract, in declaring a forfeiture, if the interest of the public do not demand such a judgment."); *People ex rel. v. Kankakee River*

WHEELER v. PULLMAN :

1892. 142 Ill. 197, 32 N. E. 4

·MR. JUSTICE SHOPE delivered the o

Without pausing to consider the grounds, is multifarious, we are of opinion that on other grounds, properly sustained, and by their bill, it was properly dismissed. It may be maintained upon either of two grounds: first, the corporation, wind up its affairs, and second, as a bill for an accounting against the Pullman Palace Car Company and

[illegible]

The necessity, for invoking the aid of a court of law, to effect the payment of forfeiture at law, that court and administer the fund, has led to courts of equity with jurisdiction to do

Improvement Co. (1882) 103 Ill. 491, 511
where public interest requires it).

To similar effect, *People v. North River*, N. Y. 582, 24 N. E. 834, 9 L. R. A. 33, 1887. "The transgression must be not merely for profit and serious; and such as to harm or injure the public. Corporations may, and often do, exceed their rights as affected. When these are adjusted, the right is averted. But, where the transgression has a tendency to the welfare of the people, they may summon the courts to their aid, if of its franchise or the violation of its corporate rights."

Cf. *People ex rel. v. Dashaway Assn.* (188 R. A. 117, where the court said, *semble*, that a ground of forfeiture, although there is no

Statement omitted. The opinion is given.

poration and to wind up its affairs in given cases, at the suit of an individual beneficiary of the fund. The power to confer such jurisdiction by statute, as one of the powers over corporations reserved by the State, has been uniformly recognized, and nowhere more clearly than in this State, (*Ward v. Farwell, et al.* 97 Ill. 593; *Chicago Mutual Life Indemnity Assn. v. Hunt*, 127 Ill. 257.). And whenever the power of the court of chancery has been properly invoked, the jurisdiction has been sustained. *Life Assn. of America v. Fassett*, 102 Ill. 315; *Chicago Life Ins. Co. v. Auditor*, 101 Ill. 82; *Mining Co. v. Mining Co.*, 116 Ill. 170, and cases supra.

By the 25th section of the statute for the incorporation of companies for pecuniary profit, being the only section applicable here, it is provided: "If any corporation, or its authorized agents, shall do or refrain from doing any act which shall subject it to a forfeiture of its charter or corporate powers, or shall allow any execution or decree of any court of record for the payment of money, after demand made by the officer, to be returned, 'No property found,' or to remain unsatisfied not less than ten days after such demand, or shall dissolve or cease doing business, leaving debts unpaid, suits in equity may be brought against all persons who were stockholders at the time, or in any way liable for the debts of the corporation, by joining the corporation in such suits," etc. And after providing for pro rata liability of stockholders upon unpaid subscriptions, etc., and for enforcing the same, proceeds: "And courts of equity shall have full power, on good cause shown, to dissolve or close up the business of any corporation, to appoint a receiver therefor," with authority to wind up its affairs.

It is not pretended that the facts alleged bring the bill within the provisions of the clause of the statute first quoted. It is not alleged, nor are facts set forth showing, that any of the causes exist for which bills in equity are by this statute authorized to be filed. The bill invokes, not the power conferred by the statute, but the general chancery powers of the court. But it is said, in effect, that as the second clause of the statute quoted gives courts of equity power to decree the dissolution of a corporation "on good cause shown," it may exercise that jurisdiction whenever the interests of the stockholders, or any of them, in equity and good conscience demand it. We do not think the statute capable of that construction. It is clear that the purpose of the provision was to enable the court, in all cases in which the jurisdiction of the court was properly invoked under the statute, to afford complete relief. By the first clause a remedy is provided by which the assets of the corporation, in the cases enumerated in the statute, may be applied in payment of its liabilities, and if insufficient therefor, that subscribers for and holders of unpaid stock of the corporation may be compelled to contribute to the payment of any balance of corporate indebtedness after the application of the corporate effects, without first procuring a judgment of forfeiture at law. No judgment forfeiting the charter of the corpora-

tion is necessary to authorize the court to afford this relief, but by the latter provision the court may, in cases where cause of forfeiture exists, declare the same, and by its decree dissolve the corporation, and through its receiver administer and distribute the corporate estate, thus making the remedy in equity, in such cases, complete. (St. Louis, etc., Mining Co. v. Mining Co., 116 Ill. 170; Alling v. Wenzel, 133 Ill. 264.) As said by this court, in construing this provision of the statute, in Chicago Mutual Life Ins. Co. v. Hunt, 127 Ill. 274: "Courts of equity are given full power, on good cause shown, as a portion of the relief provided for by that section, to dissolve or close up the business of the corporation and to appoint a receiver of its effects." We are of opinion that it is only "as a portion of the relief provided for by that section" that the power to dissolve the corporation can be invoked. Moreover, "good cause" for dissolving the corporation would necessarily be a legal cause,—a cause for which the sovereign authority might by law, resume the franchise granted. It cannot be presumed that the legislature intended, by the use of the language here employed, to authorize a decree forfeiting the corporate franchise for causes for which the state might not procure judgment of forfeiture at law. The bill is not maintainable upon this ground. * * *

*Judgment affirmed.*⁹

WILSON v. LEARY.

1897. 120 N. Car. 90, 26 S. E. 630.

CIVIL ACTION, for the recovery of land, tried before Robinson, J., at Fall Term, 1896, of BERTIE Superior Court, upon an agreed statement of facts, a jury trial being waived. The land in controversy was conveyed on the 5th day of July, 1849, by Henderson Wilson, the ancestor of plaintiffs, to trustees for Oriental Lodge, No. 24, Independent Order of Odd Fellows, which was incorporated under an Act of the General Assembly of North Carolina, at its session of 1850. The conveyance was in fee. The trustees and the Lodge went into possession and held it until 1872, when the Lodge ceased to exist, and was never revived. Under the direction of the Grand Lodge of Odd Fellows, the land was sold in 1873, to the defendants. Previous to the incorporation of Oriental Lodge by the General Assembly, it had been chartered by the Grand Lodge upon regular petition, and was one of the regularly constituted and duly organized subordinate

⁹ In re French Bank Case (1879) 53 Cal. 495; Coquard v. National Linseed Oil Co. (1898) 171 Ill. 480, 49 N. E. 563; Strong v. McCagg (1882) 55 Wis. 624, 13 N. W. 895; Conklin v. United States Shipbuilding Co. (1905) 140 Fed. 219 ("a court of equity, independent of statutory authority, cannot decree the dissolution of a corporation," referring to numerous authorities), *Accord*.

Cf. Miner v. Belle Isle Ice Co. (1892) 93 Mich. 97, 53 N. W. 218, 17 L. R. A. 412 and note.—Eds.

lodges or branches of the order. It was also agreed that the plaintiffs had never listed its property for taxation. The action was brought March 5, 1892, by the plaintiffs, as heirs at law of Henderson Wilson, the original grantor, claiming that the land reverted to them upon the extinction of the corporation. His Honor gave judgment for the plaintiffs, and defendants appealed.

CLARK, J.: The plaintiffs must recover upon the strength of their own title, and not upon defects, if any, in the title of the defendants. The conveyance by their ancestor, Henderson Wilson, was in fee simple to trustees "to convey to Oriental Lodge, No. 24, I. O. O. F., when the same shall have been incorporated by the Legislature of North Carolina." It was subsequently incorporated. Though no conveyance by such trustees to the lodge is shown, the learned counsel for the plaintiffs admitted that the Statute of Uses, 27 Henry VIII, in force in this State by virtue of our statute, executed the use without the execution of a deed. The grant to the trustees being in fee simple, the cestui que trust took in fee. *Holmes v. Holmes*, 86 N. C. 205. When the lodge ceased to exist for want of members, whether its property passed to the grand lodge of I. O. O. F. in this State, of which Oriental Lodge, No. 24, was a member, or escheated to the State for the University (Code, Sec. 2627), does not concern the plaintiffs, and is not before us. The title in fee simple had passed out of the grantor, and having vested in the Oriental Lodge, upon the extinction of the latter as a corporate entity, its property, by no just construction, could return to those whose ancestors had conveyed it in fee upon receipt of the purchase money, which he and they have kept and enjoyed.

The plaintiff's counsel insist, however, that, at the time of the conveyance, the Revised Statutes (Ch. 26, Sec. 17) provided that a corporation, unless, otherwise specially stated in its charter, had existence for only 30 years, and as there was no special provision in this charter, the grantor only parted with the property for 30 years and held a resulting trust. But the conveyance was in fee, and a corporation limited in duration can take a fee simple conveyance just as a natural being, whose existence is also limited. Either may convey away the property, and upon the death of either, without having disposed of it, the property will go to pay creditors, to heirs, to stockholders, or as an escheat, according to the circumstances, but in neither case is there any reverter to the grantors. On the death of a corporation the property is usually administered by a receiver, and on the death of a natural person, by the personal representative or passes to the heirs.

By the Constitution of North Carolina (Article VIII, Sec. 1) all corporations (if chartered since 1868) are subject to extinction at any time, or their duration can be abridged or extended, at the will of the legislature. It would now be a startling doctrine that upon the repeal of a charter, all real estate, though conveyed to the corporation absolutely in fee simple, reverts as at common law to the

original grantors, to the total exclusion of stockholders. On the contrary, such property was in fee simple, base or qualified fee, as was the case in *State—School Com. v. Kesler*, 67 N. C. 368 (1852). If there were no stockholders, then the property had escheated to the state upon such corporation becoming extinct. There was no attempt to make a receiver allowed by the Code, secs. 667-670, to take possession and sell its property, and hence no reason why they apply to a corporation which was dissolved.

It is true, it was held in an opinion by 36 N. C. 358) that by the common law a corporation by the expiration of its charter property reverted to the grantor, its property to the State, and its choses in action became void on the expiration of the charter of a corporation. To enjoin the collection of notes made payable to the debtor being absolved by the dissolution of the corporation (Thomp. Corp. § 6720) refers to this as "the barbarous rule of the common law" and notes that it has since been rejected. *Glahn v. De Rosset*, 81 N. C. 467, and in *State v. Bank of the South*, 2 Com. 307, by us. Chancellor Kent (2 Com. 307) says the common law has, in fact, become obsolete where he stoutly denied that it had ever been the common law, except as to a restricted class of cases (son, supra, Sec. 6730). The subject is treated in Gray on Perpetuities, Sections 44-51, and Lord Coke's doctrines rested on the dictum of Mr. Justice Choke, in the Prior of St. Mary's (1467), and is contrary to the only case of *Norway, Winch.* 37 (1622), though Coke referred to as law. But whatever the common law, if it was the rule at all, it was not reasonable, nor could it be approved by expectations of modern courts. The modern doctrine is "upon a dissolution the title to real property reverts to the original grantors or their heirs, and the property escheats to the state." 5 Thompson, s. 100; *Smith*, 31 Barb. 641; *Towar v. Hale*, 100 N. C. 100. Conceptions of corporations naturally of a semi-barbarous age, when they were of little significance in value and functions, by even a

Coke, and the fanciful reason given by him (Coke Lit. 13b) for the reverter of their real estate, to wit, that a conveyance to them must necessarily be a qualified or base fee, have long since become outworn and discredited. That which is termed "the common law" is simply the "right reason of the thing" in matters as to which there is no statutory enactment. When it is misconceived and wrongly declared, the common rule is equally subject to be overruled, whether it is an ancient or a recent decision. Upon the facts agreed, judgment should be entered below against the plaintiffs, dismissing their action.

*Reversed.*¹⁰

STURGES v. VANDERBILT.

1878. 73 N. Y. 384.¹¹

RAPALLO, J. This action was brought to compel the defendants to apply certain moneys received by them as stockholders of the

"In *Heath v. Barmore* (1872) 50 N. Y. 302, *accord*, Rapallo, J. said: "In so far as the plaintiff's right to recover in this action is sought to be sustained, on the ground that at common law real estate held by a corporation at the time of its dissolution reverts to the grantor, it cannot be supported * * * because the rule of law invoked by the plaintiff does not prevail in this State in respect to stock corporations. Under the provisions of 1 R. L., 248, and 1 R. S., 600, §§ 9 and 10, upon the dissolution of a corporation, the directors or managers at that time become trustees of its property (unless some other custodian is appointed), for the purpose of paying the debts of the corporation and dividing its property among its stockholders; and these provisions apply as well to the real as to the personal property of corporations. * * * Consequently, where lands are conveyed absolutely to a corporation having stockholders, no reversion or possibility of a reverter remains in the grantor." (p. 305.) See *Diamond State Iron Co. v. Husbands* (1908) 68 Atl. (Del.) 240, 8 Del. Ch. 205, and note, 8 Columbia Law Rev. 222.

But see *Mott v. Danville Seminary* (1889) 129 Ill. 403, 21 N. E. 927, and note, 3 Harv. Law Rev. 135; *Danville Seminary v. Mott* (1891) 136 Ill. 289, 28 N. E. 54 (eleemosynary corporation); *Titcomb v. Kennebunk Mutual Fire Ins. Co.* (1887) 79 Me. 315, 9 Atl. 732 (mutual insurance company without stockholders); *Mormon Church v. United States* (1889) 136 U. S. 1, 34 L. ed. 481, 10 Sup. Ct. 792. In the last cited case, Mr. Justice Bradley said: "When a business corporation, instituted for the purposes of gain, or private interest, is dissolved, the modern doctrine is, that its property, after payment of its debts, equitably belongs to its stockholders. But this doctrine has never been extended to public or charitable corporations. As to these, the ancient and established rule prevails, namely: that when a corporation is dissolved, its personal property, like that of a man dying without heirs, ceases to be the subject of private ownership, and becomes subject to the disposal of the sovereign authority; whilst its real estate reverts or escheats to the grantor or donor, unless some other course of devolution has been directed by positive law, though still subject as we shall hereafter see to the charitable use. To this rule the corporation in question (the Church of Jesus Christ of Latter-Day Saints) was undoubtedly subject." (page 47.)

See also *Davis v. Memphis &c. R. Co.* (1888) 87 Ala. 633, 6 So. 140; *Have-meyer v. Superior Court* (1890) 84 Cal. 327, 24 Pac. 121, 10 L. R. A. 627; *Erie &c. R. Co. v. Casey* (1856) 26 Pa. St. 287; *Insurance Co. v. Dunscomb* (1902) 108 Tenn. 724, 69 S. W. 345.—Eds.

¹¹ Portion of opinion omitted.—Eds.

case there was no attempt to continue the action pursuant to the laws of either State.

It is further claimed, that, until a corporation is declared dissolved by judicial decree, creditors may proceed against it by its corporate name, and that it remains *in esse* until formally adjudged dissolved. All the cases cited in support of this proposition relate to a dissolution in consequence of insolvency or non-user or mis-user of the corporate franchises, or some other cause of forfeiture. In such cases, it is well-settled that the dissolution does not take effect until judicially declared. But the principle upon which that class of cases rests is not applicable to a dissolution by expiration of the charter. The dissolution in such a case is declared by the act of the Legislature itself. The limited time of existence has expired and no judicial determination of that fact is requisite. The corporation is de facto dead. (*People v. Walker*, 17 N. Y. 503; *Greeley v. Smith*, 3 Story C. C. R., 658.) Where the charter of a corporation is annulled by act of the Legislature, the corporation is extinct and no judgment can be rendered against it. (*Mumma v. Potomac Co.*, 8 Pet., 286; *Merrill v. Suffolk Bk.*, 31 Me., 57.) We have been referred to no authority holding a contrary doctrine.¹²

COULTER v. ROBERTSON.

1852. 24 Miss. 278.¹³

THIS action was founded on the promissory note of the testator of the plaintiffs in error, executed to, and held by, the Commercial Bank at Natchez. Prior to the institution of the suit, an information in the nature of a quo warranto, had been instituted against the bank, under which its charter had been declared forfeited, and the corporation was judicially dissolved, in pursuance of an act of the legislature of Mississippi, passed in July, 1843. Under the provisions of the eighth section of that act, William Robertson was appointed trustee for the purposes set forth in said section, which is in the following words, namely:

"Sec. 8. Be it further enacted, That upon judgment or forfeiture against any bank or banks, corporation or corporations, person or persons pretending to exercise corporate powers in this State, as contemplated by this act, the debtors of such bank or banks, corporation or corporations, person or persons pretending to exercise corporate privileges, shall not be released by such judgment from their debts and liabilities to the same; but it shall be the duty of the court

¹² To similar effect, see *Venable Bros. v. Southern Granite Co.* (1910) 135 Ga. 508, 69 S. E. 822. See also *Bradley v. Reppell* (1896) 133 Mo. 545, 32 S. W. 645, 34 S. W. 841, 54 Am. St. 685. Cf. *Bushnell v. Consolidated Ice Machine Co.* (1891) 138 Ill. 67, 27 N. E. 596.—Eds.

¹³ A portion only of the opinion is given.—Eds.

rendering judgment, to appoint one or more trustees to take charge of the books and assets of the same; to sue for and collect all debts due such bank or banks, corporation or corporations, person or persons pretending to exercise corporate powers, and to sell and dispose of all property owned by such bank or banks, corporation or corporations, person or persons pretending to exercise corporate powers, or held by others for its or their use, and the proceeds of the debts, when collected, and of the property when sold, to apply as may hereafter be directed by law to the payment of the debts of such bank or banks, corporation or corporations, or persons pretending to exercise corporate powers. Provided further, that the notes of any such bank or banks, corporation or corporations, or others pretending to exercise corporate power, shall at all times be received in payment of any debts due the same." Hutch. Code, 331.

This action is brought by said trustee, to recover the amount of said promissory note; the declaration setting forth the judgment of forfeiture, the appointment of the trustee, &c.

The questions for consideration are presented in two pleas: 1st. That after the appointment of said trustee, and before the commencement of this suit, the trustee had collected and received of the debts and effects of the said bank, an amount of money sufficient to pay all debts of said bank, wherewith he had paid the same, and had also collected an amount of money sufficient to pay and discharge all costs, charges, and expenses incident to this trust, &c.

2d. That in the matter of the proceedings in Adams circuit court, in which said trustee was appointed, and at the November term, 1846, of said court, said trustee made and returned to said court a schedule of the effects and evidences of debt of said bank, in his hands, and thereupon, on the motion of the district attorney for said court, it was ordered and adjudged by said court, that said trustee should sell to the highest bidder, for cash, said property and evidences of debt, embracing the note here sued on; which judgment remains in full force and unreversed.

The plaintiff below demurred generally to these pleas, and the court below sustained the demurrers and rendered judgment for the trustee; and, thereupon, the case is brought to this court by writ of error, and the matter for determination is, whether either of these pleas presents a valid defence to the action.

The opinion of the court was delivered by MR. CHIEF JUSTICE SMITH.

A judgment of forfeiture was pronounced against the late Commercial Bank of Natchez upon an information in the nature of a quo warranto, instituted under the provisions of the statute regulating the mode of proceeding against incorporated banks for a violation of their charters.

William Robertson was appointed trustee, and as such brought suit against the plaintiffs in error, on a note made by their testator,

which was the property of the dissolved corporation, at the time when the judgment of forfeiture was rendered.

The demurrer to the second and third pleas of the defendants in the court below, presents the questions which it becomes our duty to investigate. For the present, we will direct our attention to that which arises on the demurrer to the second plea. In its general form, the question thus raised is this: Had Robertson, the trustee, title to sue? Could he maintain an action on the note?

In the discussion of this proposition, two points of inquiry naturally suggest themselves. 1st. Whether a full payment of the debts due by the bank, at the date of its dissolution, or the collection from the assets of an amount of money sufficient for that purpose by the trustee, was a full and complete execution of his trust, whereby he became *functus officio*? 2d. Whether the trusts which had vested in Robertson were, in reality, terminated by the payment of the whole of the debts of the bank, or by the collection of funds by him sufficient for that purpose, such matter constituted the basis of a valid defence, of which the defendants below had a right to avail themselves in bar of a recovery?

1. The effects or consequences at common law of a judgment of forfeiture, rendered against a corporation, have been materially modified by the legislation of this State. Hence, to enable us to respond to the first inquiry a distinct perception, as well of the consequences which followed at common law upon a judgment of forfeiture against a corporation, as of the changes produced by the statutes of our own State, is essential.

The elementary books and the numerous cases decided, are uniform in their language in regard to the consequences resulting from the dissolution of a corporation. They held that, upon the death of a corporation, all its real estate remaining unsold, reverts back to the original grantor and his heirs. The debts due to and from the corporation are all extinguished. Neither the stockholders, nor the directors, nor trustees of the corporation, can recover those debts, or be chargeable with them in their natural character. All the personal estate of the corporation vests in the crown, with us, in the people of the State, as succeeding, in this respect, to the rights and prerogatives of the king. *Co. Lit.* 13b; 1 *Black. Comm.* 484; *Angell & Ames on Corp.* 513; 3 *Burr. Rep.* 1868; *Commercial Bank v. Lockwood*, 2 *Harr.* 8; 1 *Blackf. Rep.* 283; *Fox v. Horah*, 1 *N. C. Rep.* 353; 2 *Kent, Comm.* 309.

This we understand to be the settled doctrine of this court. It was said by the late learned chief justice, in delivering the opinion of the court, in the case of the *Commercial Bank of Natchez v. Chambers*, that it had been urged "in argument with much plausibility, that even without the interposition of the legislature, the debts due to and from the bank would have survived its dissolution; that these commercial corporations should be regarded as partnerships, and the fund or property owned by them a trust fund which equity would

appropriate to the payment of their debts seems to have fallen into a different category, regarded as a settled doctrine, that on the part of a corporation, the debts due to and from it are subject to an implied condition in the contract, that there is no person in whose favor or against whom they are enforced."

Following the suggestion to which the court gave a reply, counsel upon the argument of the case sustained the assumption with great ingenuity. The contracts entered into by a corporation, though dissolved, but continues unimpaired. And even if they cannot be enforced is this, there is no loss of the legal title vests. In other words, the remedy is lost, but the remedy has been lost by the corporation.

We do not assent to the proposition, tained by authority. There is an obvious credits or debts due by contract unac property, either general or special, and chattels. The latter are matters of substance, an ideal being, but an actual existence; independent of any ownership, either in being not essential to their existence that there are not annihilated by the extinction of the previously belonged, but pass upon its death those who may take them. "As they remain the subjects of occupancy and possession, can lay hold of them, and the State, they take possession of the goods and chattels of a corporation. But such is not the conditioning to such corporation; they are merely things—they have an ideal but not an actual existence, tangible nor the subjects of occupancy or possession." 13. A debtor and a creditor are essential to a debt. There can be neither a debt nor a creditor, be in actual being or in expectancy without actual existence, a person by whom the duty performed, as well as a person who is of the debt, or accept the performance of the debt; therefore, the payer or payee, the debtor or creditor by whom a duty is to be performed, or the thing which is to be done, ceases to exist with the legal possibility of a representative, the thing does not exist, and the obligation of payment or performance ends.

The case above referred to of the Com
Chambers, is cited to show that the oblig

dissolved corporation survives its dissolution. The passage quoted from the opinion in that case distinctly announces the principle as the settled doctrine of our courts, that the debts due to and by a corporation upon its dissolution are extinguished. Not such is the condition of a debt where the debtor and creditor survive, but which has been barred by the statute of limitations. The legal remedy has been lost, but the moral right to demand payment and the obligation to pay remain. If the effect of the statute of limitations were held to extinguish the right as well as to bar the remedy, it is manifest that a subsequent promise to pay the debt would be void for want of consideration. For it must be perfectly immaterial whether if a right or debt is extinguished, the effect is produced by a statute bar, the civil or natural death of one of the parties to the contract, or by a payment itself.

The case of *Mumma v. The Potomac Company*, 8 Peters' Rep. 281, has been cited for the same purpose. Mumma, the plaintiff in that case, was a judgment creditor of the Potomac Company, and after its dissolution, which was affected by a surrender of its charter, issued out a writ of *scire facias* to revive his judgment. The questions presented by the record in that case were, 1st. Whether the corporate existence of the company was not destroyed so as to defeat the rights and remedies of its creditors? 2d. Whether the deed of surrender did not violate the contracts of the company, and whether the legislative acts of Virginia and Maryland, though confirmed by the act of congress, were not on that account void? Both questions were decided against Mumma, and Judge Story, who delivered the opinion of the court, in discussing the second point says: "The obligation of those contracts, (the contracts of the defunct corporation,) survives, and the creditors may enforce their claims against any property belonging to the corporation, which has not passed into the hands of bona fide purchasers, but is still held in trust for the company or the stockholders thereof, at the time of its dissolution, in any mode permitted by the local laws." This case was cited in the opinion of this court in *Nevitt v. The Port Gibson Bank*, and appears to have been regarded as an authority in support of the position, that the obligation of contracts entered into by and with corporations survive their dissolution. We think upon examination it will be perceived that the import of the decision was misunderstood, and that Judge Story was very far from intending to intimate that according to the common law, upon the dissolution of a corporation, the debts due to and by it would not be extinguished.

The pleadings in that case showed that the Potomac Company, in pursuance and in execution of the provisions of the charter of the Chesapeake and Ohio Canal Company, chartered by the States of Maryland, Virginia, and by the Congress of the United States, had conveyed in due form of law to the said company, all of its property, rights, and privileges of every description whatever; and had, also, in due form, made a surrender of its charter; which transfer and

DISSOLUTION

surrender was accepted by the Chesapeake acts incorporating this latter company, signment or conveyance was for the benefit of the holders. Upon the acceptance of the assignment attached to the property assigned in the act of the Ohio Canal Company in favor of the company; whose debts or claims against the company were extinguished by the provisions of the act of the Chesapeake and Ohio Canal Company. Hence, it was very proper for the judge, that "the creditors of the Potomac Company, whose claims against any property bequeathed to which had not passed into the hands of the company was still held in trust for the company at the time of its dissolution, in any mode of distribution." Besides the twelfth section of the act of the Chesapeake and Ohio Canal Company, makes it the duty of the directors of that company, so long as the company is a creditor of the Potomac Company, to withhold dividends against the same in the stock of the Chesapeake and Ohio Canal Company, (which the act enables the directors to do annually, such dividends to be paid out of the amount of the revenues of the Potomac Company for the last five years preceding the organization of the Chesapeake and Ohio Canal Company, as the directors may determine at that time may bear to the supposed aggregate amount of the debts of the Potomac Company. "So that," continues the judge, "here is no question of distributing the assets of the company, but of apportionment of its revenues, in the manner in which is practically done upon its dissolution." The property of the whole property of the Potomac Company, as the Chesapeake and Ohio Canal Company, upon the terms of the act, who held it in trust for the creditors of the Potomac Company, whose assets were looked to in making the arrangement for the company, materially different in principle from a corporation, of its effects, for the payment of its debts, and when, after the assignment, its debts were paid by either a surrender, a judicial sale, or a liquidation.

Considering it conclusively settled, the position upon the dissolution of a banking corporation, and by it are extinguished, we will determine to what extent and for what purposes the rules of law applicable to that subject have been modified by the

(The learned court proceeded to decide on July 26th, 1843, which provided for a trial

the benefit of the creditors of a corporation did not give the trustee any power to collect debts for the benefit of the stockholders.)¹⁴

HASTINGS CORPORATION v. LETTON.

1907. L. R. (1908) 1 K. B. 378.¹⁵

APPEAL from the county court of Sussex holden at Hastings, which gave judgment for the plaintiffs. The facts sufficiently appear in the opinion.

DARLING, J.—This case raises a difficult point which, apparently for the first time, it is necessary to decide. The corporation of the borough of Hastings granted a lease to a certain company, who covenanted in the lease to pay the rent thereby reserved for the term of seven years. The appellants entered into similar covenants as sureties. The company assigned the lease to another company, the Southern Produce Company, Limited, the appellants remaining sureties on the same terms for the new company, and the old company ultimately dissolved. The new company, the assignees of the lease, also dissolved, namely, in August, 1906, without having assigned over the lease; and the question is whether, the new company having become dissolved, the appellants are nevertheless still liable to pay the rent to the lessors. They undertook to pay the rent in these terms: "The lessees do, and each of the sureties doth for himself covenant that the lessees and sureties, or some or one of them, will during the said term pay the said rent on the dates and in the manner hereinbefore mentioned." The question is whether the term came to an end by the dissolution of the new company or

¹⁴ *Bank of Mississippi v. Duncan* (1878) 56 Miss. 166, 173; *Fox v. Horah* (1841) 36 N. Car. (1 Ired. Eq.) 358, 36 Am. Dec. 48, *Accord*. The latter case was declared to be overruled in *Wilson v. Leary*, *supra*. See Cook, Corps. (6th ed.), sec. 641.

In *re Higginson & Dean* (1898) L. R. (1899) 1 Q. B. Div. 325, *held* that the dividend upon the debt of a corporation which was dissolved after proof of the debt had been filed in a bankruptcy proceeding was not distributable among the other creditors, but passed to the Crown as *bona vacantia*. See notes, 12 Harv. Law Rev. 558, 15 *id.* 743. At pages 330-1, Wright, J. said: "The authorities for the proposition that on the dissolution of a corporation aggregate debts due to or from it are extinguished are by no means clear or satisfactory. * * * 'The debts of a corporation (Blackstone says), either to or from it, are totally extinguished by its dissolution; so that the members thereof cannot recover or be charged with them, in their natural capacities; agreeably to that maxim of the civil law, *si quid universitati debetur, singulis non debetur; nec, quod debet universitas, singuli debent*'. The American decision in the case of *The State Bank v. The State* (1 Blackf. Ind. Rep. 267) relies on those authorities as supporting the general proposition, but it does not advert to this qualification, or add new references to authority, and the authorities cited do not in any way support the proposition, except as so qualified."—Eds.

¹⁵ Statement abridged. Concurring opinion of Phillimore, J., omitted.—Eds.

whether it still exists, and, if it does are still bound to pay the rent although signees are gone out of existence. That the sureties are still bound to pay the dissolution of a company is an analogy; he argues that if a single lease term of years and the payment of sureties, the sureties would continue term notwithstanding that the lessee died a bastard without issue and intestate court judge says with truth, the term would still subsist and vest in the corporation undertaken to pay the rent during the term the sureties would be liable for analogy, though specious, is false. That is in truth but a figurative expression in the Companies Act, 1862; the word is not dissolution. In the case of a company upon it, as death does upon a human being, liabilities and property still on its behalf. A company is regulated by ss. 142 and 143 of the Companies Act, 1862, in which it is provided that before a company can be dissolved it must first be divested of its property; it must first be divested of its property to dissolve until it is divested of every thing. The county court judge has based his decision on these facts. A truer analogy, though not a perfect one, would be the case of a single lease. On the death of such a lessee the lease passes from Blackstone's Commentaries to the appellants is still good law. Part of the argument in *re Higginson and Dean*, (1899) 1 Q. B. 101, is a statement of the law in modern times. "But the body politic may also itself die, which dissolution is the civil death of the corporation. In this case their lands and tenements shall remain in the hands of those who granted them to the corporation on the condition to every such grant, that if the grantor shall have the lands again, the grant shall fail. The grant is indeed a lease for years, which may endure for ever, but it is determined by the dissolution of the body politic, and it shall go back by reversion, as in the case of a lease for years. Bl. Com. 484. The law there laid down is the same. I cannot see that when there were any bona vacantia to vest in the crown, and the land reverted to the grantor, or to his heirs, in his reversion, and he has his whole estate, the authority is wanted it will be found in the law." (1899) 1 Q. B. 101.

(1899) 1 Q. B. 325, at p. 332, where Wright, J., after quoting the opinion of Story J. in the cases of *Wood v. Dummer* (1824) 3 Mason, 308 and *Mumma v. Potomac Co.* (1834) 8 Peters, 281, said: "This statement of the law may not perhaps be entirely applicable in this country, but it requires consideration. It might be reasonable to enact"—I pause there to observe that the learned judge says, "to enact," not "to hold"—"that, in analogy to the immemorial law of executors and administrators, and the statute of 31 Edw. 3, st. 1, c. 11, on the dissolution of a corporation aggregate all its rights, including its rights of action on executed contracts, such as those evidenced by bank notes or bonds, or on claims in debt, devolve upon the Crown, subject to payment of the corporation's own debts. It would, however, I think, in the present state of the authorities, be judicial legislation to declare the Crown entitled to maintain actions in such cases except where it can allege a trust." In the present case I think it would be judicial legislation to hold that the law as laid down by Sir W. Blackstone does not apply, and that when a company, being lessees or assignees of a term of years, ceases to exist, the term does not revert to the grantor.

*For these reasons I think this appeal should be allowed.*¹⁸

¹⁸ The intended appeal was not pursued. See note criticizing the principal case, 8 Columbia Law Rev. 410.—Eds.

INDEX.

[References are to Pages.]

A

ACCEPTANCE,
of charter, 114, 115, 119.

ASSAULT AND BATTERY,
corporate liability for, 12, 14.

ASSETS,
See CAPITAL STOCK; TRUST FUND.

ASSIGNMENT,
right of corporation to make, for benefit of creditors, 232.
who can make, for benefit of creditors, 428.

ATTACHMENT,
of shares of stock, as against unrecorded transferees, 752, 757.

ATTORNEY, POWER OF,
See TRANSFER OF STOCK.
right of innocent holder of certificate of shares delivered under blank,
in fraud of owner, 757, 763, 766, 769.
certificate therewith, stolen, 764.
when new certificates issued, 770, 772.
rights of owner of certificate, how effected by forgery of, authorizing
transfer, 770, 772.
rights and liabilities of holder of certificate issued on forged, 772, 778.
rights and liabilities of corporation on certificate issued on forged,
770, 772, 778.

B

BANKRUPTCY,
treatment of doctrine of corporate entity in, 46.

BONUS,
of stock with bond issue, 830, 834.

BORROW,
power of corporation to, 230.

[References are to Pages.]

BY-LAWS,

See STOCKHOLDERS.

power of corporation to make, 232, 546, 548.
 power to amend, 450.
 validity of, 544, 610.
 who can make, 539, 541.
 restraining transfer of shares, 726, 735.
 affecting right to vote, 523.
 function of, 540, 543, 547, 607.
 effect of, on third parties, 541, 544.
 creation of lien on stock by, 548, 730.

C

CAPITAL STOCK,

See SHARES OF STOCK; PREFERRED STOCK; WATERED STOCK.

nature of, 109, 632, 836, 847.
 distinguished from property of corporation, 559.
 distinguished from shares of stock, 106, 109, 513.
 right to increase amount of, 561, 584, 588, 837.
 right to reduce amount of, 212.
 power of directors to increase or reduce, 422, 428.
 taxation of, 109.
 subscription to, and payment of, as conditions precedent to corporate existence, 124, 128.
 payment for increased, 365.
 subscription of entire as condition precedent to subscriber's liability, 388, 391, 395.
 overissue of, 619, 622.

CERTIFICATES OF STOCK,

distinguished from capital stock, 358.
 necessity of tender of, before payment for stock due, 360, 361.
 when delivery of, unnecessary, 735.
 effect of loss of, 764.
 as approximating negotiable securities, 756, 757, 763.

CHARTER,

See STATE CONTROL.

acceptance of, 114, 119.
 acceptance without the state invalid, 115.
 acceptance, time of, 115.
 acceptance, place of, 115.
 acceptance, method of, 115.
 revocability of offer of, 115, 942.
 effect of expiration of, 958.
 as a contract, 72, 75, 609.

[References are to Pages.]

CHARTER—Continued.

- constitutionality of general laws, 116.
- obtaining, in two or more states, 135, 136, 138, 140, 148.
- effect of amendment of, on stock subscription, 412, 416, 420.
- surrender of, 943, 944.
- what constitutes, under general laws, 122.

CITIZEN,

- corporation as, for purpose of Federal jurisdiction, 81, 85.
- corporation as, under Art. 4, sec. 2, of Fed. Constitution, 85.
- corporation as, under 14th Amendment of Fed. Constitution, 85.
- joint-stock company as, 93.
- presumption of citizenship of shareholders, 84, 124.
- effect of Incorporation in two or more states, 142.

CONSOLIDATION,
effects of, 136.

CONTEMPT,
corporate liability for, 22.

CONTRACT,

See **ULTRA VIRES CONTRACTS; PROMOTERS; DIRECTORS.**

- of corporation distinct from that of shareholders, 3.
- power of corporation to, 230.
- charter as a, 67, 72, 75.

CO-PARTNERSHIP,

See **PARTNERSHIP.**

CORPORATION,

- distinction between joint-stock company and, 89, 93, 94.
- distinction between *de jure* and *de facto*, 130, 184, 194, 385.
- citizenship of, 81, 85.
- classification of, 73.
- effect of legislative declaration that company is not, 89.
- as an entity distinct from stockholders, 3, 6, 8, 37, 43, 51, 53, 76, 669, 692.
- general attributes of, 1, 8, 69, 76, 692, 867.
- as trustee for stockholders, 716, 723.
- individual liability consistent with concept of, 86, 101.
- power of, to subscribe for stock, 387.
- power of, to release subscriber, 397.
- must act through agents, 453, 491, 943.

CORPORATION TAX,

- application of Federal, 105.

[References are to Pages.]

CREATION,

necessity of legislative authority for, 119.
by letters-patent, 114.
by prescription, 114.
by parliament, 114.
by special act, 114, 948.
under general laws, 119, 121, 122.
delegation of right of, 114, 116.
invalidity of, by agreement alone, 119, 167.
authorized objects, 121.
typical method of, 125.
conditions precedent, 124, 128.
directory and mandatory provisions, 130, 132.
under laws of two or more states, 132, 137, 140, 146.
memorandum and articles of association distinguished, 280, 600.

CREDITORS,

See SHAREHOLDERS; DIRECTORS; TRUST FUND.

relation between, and corporation, 780, 785.
equity jurisdiction over corporate property at suit of an unsecured,
with claim not reduced to judgment, 789.
right of insolvent corporation to prefer, 793.
right of, to require a reconveyance of property fraudulently obtained, 785.
right of, to compel payment by shareholder of difference between subscription and par value, 625, 830, 840.
right of, where subscription to stock is sought to be avoided, 828, 830.
right of, in distribution of assets of corporation, 951.
right of, prior, against shareholders, 841, 847.
right of, subsequent, with knowledge, 849, 856.
right of, where directors have been given security by insolvent corporation for advances, 812.
right of, where directors have accepted deposits after insolvency, 806.
right of, where directors have been accorded a preference by insolvent corporation, 810.
right of, in equity on dissolution, 951, 956.
right of, to restrain corporation, 800, 801.
right of, against subscribers, 368, 823.
right of, against holders of over-issued stock, 622.
right of, against holders of bonus stock, 628, 838, 848.
right of, against holders of stock issued for money at less than par, 830, 834, 841, 842.
right of, against holders of stock issued for property at an overvaluation, 850, 852, 853.
extent of liability of shareholder to, for assets withdrawn from, or subscriptions owing to, corporation, 785, 825.
suit by, against stockholders, 785, 788, 823.
effect of repeal of statutory liability of directors to, 821.

[References are to

CREDITORS—Continued.

- right of, to recover dividend paid to holder, 795, 799.
- right of, to sue in foreign jurisdiction to enforce statutory liability, 816.
- nature of statutory liability of stockholder, extent of statutory liability of stockholder, conditions precedent to enforcement of liability of stockholder to, 860.
- right of, to enforce statutory liability of stockholder, 865, 869, 873, 878.
- when statutory liability of shareholder is enforced, 873, 878.
- as to what claims statutory liability of stockholder is enforced, 880.
- who is shareholder, for purpose of enforcing liability, 898, 901.

CRIMES,

- corporate liability for, 16, 20, 22, 23.

D

DAMAGES,

- corporate liability for punitive, 14, 21.

DEBTS,

- right of corporation to contract, 230.

DE FACTO CORPORATIONS,

- requisites of, 149, 150, 157, 160, 165, 166.
- meaning of term, 160.
- as a reality, 187.
- distinguished from estoppel to deny existence, cannot be questioned collaterally, 149.
- doctrine of, rests on public policy, 191.
- proof of user required, 150, 166, 193.
- immunity of associates in, from individual partnership liability of associates in, under expired law, 176.
- under unconstitutional law, 156, 172.
- under no law, 176.
- under void law, 176.
- existence in absence of estoppel, 165.
- effect of want of good faith, 168.
- power to sue for trespass, 179, 182.
- tort liability of associates in, 182.
- power to exercise right of eminent domain as a conduit of title, 184.
- subscription to stock in, 384, 387.

[References are to Pages.]

DE JURE CORPORATIONS,

defined, 385, 475, 491.

DELEGATION OF POWERS,

by legislature of right to create corporation, 116.

by king of right to create corporation, 114.

by directors, 451.

by stockholders, 449.

DIRECTORS,

as managers, 425, 429, 491, 669.

as fiduciaries of corporation, 449, 508, 720.

as trustees, 449, 452, 456, 459, 471, 493, 497, 514, 669.

degree of care required of, 471, 476, 477, 481, 489, 490.

liability of, for error of judgment, 463, 482.

liability of, for unauthorized acts, 415, 459, 464, 689.

liability of, for acts of co-directors, 509.

liability of, where corporate organization imperfect, 129.

liability of, criminally, 464, 466, 475.

liability of, for secret profits, 509.

good faith of, as defense for misuse of assets, 463, 471, 482, 689, 726.

breach of trust by, 474, 490, 508, 509.

review of business judgment of, in equity, 459, 578.

when vested with exclusive power, 428.

must act as a board, 433.

validity of informal acts of, 439.

source of authority of, 440.

abdication of powers to officer by, 441.

removal of, 445, 450.

increase in number of, 450.

more than figure-heads, 484, 491.

gross negligence of, 490.

contracts between corporations with interlocking, 494, 499, 501.

ratification by stockholders of corporate contracts with, 494.

holding of stock as affecting eligibility of, 748.

effect of knowledge by co-directors of improper conduct of, 508.

duty of, to declare dividends, 574, 578.

general extent of powers of, 422, 425, 428.

power of, to lease, 428.

power of, to mortgage, 428.

power of, to compromise, 428.

power of, to make assignment for benefit of creditors, 428.

power of, to increase capital stock, 428.

power of, to make by-laws, 541.

power of, to admit insolvency, 428.

power of, to declare dividends, 562, 578.

power of, to accept amendment of charter, 428.

power of, to assume debt of third person, 428.

*[References are to Pages.]***DIRECTORS—Continued.**

- power of, to change nature of corporate business, 428.
- power of, to delegate authority, 451.
- power of, to create executive committee, 451.
- power of, to release subscribers, 394, 397, 428.
- right of, to contract with corporation, 459, 491, 494, 496, 499, 502.
- right of, to lend money or credit to corporation, 502, 505.
- right of, to compensation, 450, 459, 927.
- right of, to purchase corporate property at foreclosure sale, 502, 505.
- right of, to indemnity, 454, 457.
- right of, to purchase corporate obligations, 505, 507.
- right of, to purchase shareholder's stock, 510, 515, 518.
- relation of, to individual stockholder, 510, 512, 515, 518.
- relation of, to stockholders as a body, 512, 513, 720.
- relation of, to creditors at common law, 801, 806, 810, 812.
- relation of, to creditors by statute, 816, 822.

DIRECTORY PROVISIONS,

- effect of non-compliance with, 129.
- distinguished from mandatory, 130, 132.

DISCOUNT,

- issue of shares at a, 622, 625.

DISREGARD OF CORPORATE ENTITY,

See **LEGAL ENTITY.**

DISSOLUTION,

- proceeding brought by state for, 948, 951.
- methods of, 940, 942, 952, 956, 958.
- waiver of right to insist upon, 947.
- effect of abandonment of business, 944, 945.
- effect of insolvency, 943, 952.
- effect of omission to elect directors, 943.
- effect of death of all members, 942, 944.
- effect of disposal of all corporate property, 794, 943, 945.
- power of equity to decree, 951, 953.
- when statute elucidating causes for, is self-executing, 946, 948.
- who to determine whether cause for, 949.
- what must be shown beyond charter violation, 949, 951.
- exercise of discretion in proceedings for, 950, 951.
- effect of, upon real property, 940, 953, 956.
- effect of, upon personal property, 955, 960, 964.
- effect of, upon leases, 964.
- effect of, upon debts, 955, 958, 963.
- effect of, upon suits, 956.

[References are to Pages.]

DIVIDENDS,

See **PREFERRED STOCK.**

- nature of, 550.
- as a debt, 550, 564, 566.
- burden of loss where fund set aside for the payment of, is lost, 563, 565.
- source of, 551, 554, 557.
- declaration of stock or property, 557, 563.
- how declared, 567, 570.
- revocability of vote declaring, 567, 570.
- right of stockholders to share alike in, 568.
- equity jurisdiction to compel declaration of, 574, 578.
- declared out of capital, 551, 556, 558.
- who entitled to, 571, 573, 574.
- between life-tenant and remainderman, 574.
- when a trust fund, 564, 566, 569.
- custom as affecting right to, 572.
- payment of, by corporation after notice, to one not entitled, 574.

E

ELEEMOSYNARY CORPORATIONS,

- characteristics of, 73.
- disposal of property of, on dissolution, 956.

EMINENT DOMAIN,

- exercise of right of, by de facto corporation, 182, 184, 192.

ENTITY,

See **LEGAL ENTITY.**

ESTOPPEL,

- to deny corporate existence, 149, 155, 177, 193.
- where dealing has been on corporate basis, 167, 172.
- in ultra vires contracts, 293, 312, 339.
- in ultra vires torts, 353.
- in stock transfers, 759, 770.

EXECUTIVE COMMITTEE,

- delegation of power of directors to, 451.

F

FEES,

- payment of, as condition precedent to corporate existence, 168.

FICTION OF CORPORATE ENTITY,

- denial of truth of, 66.
- disregard of, 37, 50, 51, 54.
- nature of, 53.

FICTITIOUS STOCK,

See WATERED STOCK.

FOREIGN CORPORATIONS,

status of, 868.

right of state to impose conditions upon, 85.

FORFEITURE,

of shares, for non-payment, 392, 750.

of charter, for issue of watered stock, 639.

of charter, for abuse, 940, 943, 950.

necessity of judicial decree of, 943.

when self-executing, 947, 948.

for usurpation of franchise, 951.

FORMATION,

See CREATION.

FRANCHISE,

nature of, 76, 119.

power of corporation to hold, 231.

in whom vested, 77, 110.

assignability of, 77, 78, 267.

G

GENERAL LAWS,

formation of corporations under, 114.

necessity for, 119.

nature of franchise under, 119.

GUARANTOR,

power of corporation to be, 231.

I

INDEMNITY,

See DIRECTOR; TRANSFER OF STOCK.

INHABITANT,

corporation as an, 85.

INSPECTION,

of corporate books and records, 592, 594.

right of, how affected by bad faith, 594, 596.

with expert assistance, 594.

right to make transcript, 594.

effect of statute on right of, 596.

[References are to Pages.]

J

JOINT-STOCK COMPANY,

- distinction between corporation and, 89, 93, 94, 103.
- as possessor of corporate attributes, 104.
- status of, under Federal Corporation Tax, 105.
- when treated as partnership, 91.

JUDGMENT,

- validity of, when against corporation after dissolution, 956.

JURISDICTION,

- effect of fraudulent incorporation on, 33.

L

LEGAL ENTITY,

- corporation as a, 3, 5, 43, 66, 76, 442, 813, 925.
- Roman view of, 6.
- disregard of doctrine of, 2, 15, 26, 28, 32, 37, 49, 54, 62, 65, 924.

LIBEL,

- corporate liability for, 11.
- liability of directors for, 689.

LIEN,

- upon stock, 548, 730, 735.

M

MAJORITY,

- powers of, 672, 694, 708, 716, 719.
- fraudulent acts by, 672, 707, 714.
- unauthorized acts by, 694.
- profit by, at expense of minority, 704, 714, 716.
- duty of single shareholder in, 707, 717, 722, 724, 726.
- exercise of ratifying power by, 713, 715.
- as trustee for minority, 724.

MALICIOUS PROSECUTION,

- corporate liability for, 11.

MANDAMUS,

- to test right of director to office, 450.
- to obtain inspection of corporate books and papers, 595.
- to obtain payment of dividend declared, 564.

MANSLAUGHTER,

- corporate liability for, 22.

[References are to Pages.]

MEETINGS,

See VOTING.

validity of, 129.

MORTGAGE,

power of corporation to execute, 231.

power of corporation to execute for future advances, 231.

power of corporation owing public duties to, 231.

N

NATIONAL BANKS,

taxation of shares in, 113.

ultra vires conveyances to, 237, 305.

lien on stock in, 730.

NEGOTIABLE PAPER,

power of corporation to issue, 230.

power of corporation to issue accommodation, 233.

liability of corporation to holders of accommodation paper, 233

effect of consent of shareholders on accommodation paper, 233.

NUISANCE,

corporate liability for, 22.

O

OBSCENE MATTER,

criminal liability of corporation for mailing, 23.

OFFICERS,

powers of, 441, 444.

right of, to buy shareholder's stock, 510, 514, 515, 518.

necessity of, 943.

de facto, 181.

compensation to, 453, 454, 458.

liability of, where corporate organization imperfect, 129.

ONE-MAN COMPANY,

nature of, 45, 46.

ORGANIZATION,

See CREATION.

P

PARTNERSHIP,

distinguished from corporation, 86, 90, 94, 244, 641, 728.

power of corporation to enter into a, 218, 222, 224.

corporate directors contrasted with managing partners in a, 432, 587.

62—PRIVATE CORP.

15

[References are to Pages.]

PERSON,

stockholders considered as a, 1, 5, 8.

POWERS OF A CORPORATION,

scope of implied, 69, 196, 209, 229.

distinction between excess and abuse of, 304.

to engage in a distinct business, 199, 204, 208, 230, 233, 276, 292, 310.

to engage in a business auxiliary to main corporate business, 198, 208, 209.

to purchase property, 196, 231.

to alien property, 196, 231, 267, 694.

to alien all its property, 224, 227, 229, 694, 708.

to sue and be sued, 196.

to contract, 230.

to have a seal, 196, 230.

to make by-laws, 232.

to acquire its own shares, 209, 211, 212, 214.

to acquire shares in other corporations, 215, 216, 218, 244, 245, 286.

to enter into a co-partnership, 218, 222, 224.

to enter into a joint transportation agreement, 224.

to borrow money, 230, 231, 606.

to issue negotiable paper, 230.

to make or indorse accommodation paper, 233.

to hold a fee simple, 231.

to hold a franchise, 231.

to pledge or mortgage, 231, 267.

to lend money, 231.

to act as surety or guarantor, 231, 232.

to act as trustee, 232, 804.

to make assignment for benefit of creditors, 232.

to prefer creditors, 232.

to take by bequest, 232.

to take by devise, 232.

to subscribe to exhibition funds, 233.

to maintain relief fund for employees, 233.

to practise law, 233.

to practise medicine, 233.

to contribute to political campaign funds, 233, 464.

to vote stock held by, 719.

of foreign corporations, 232.

incidental or consequential, 198, 203, 206, 208, 209.

test of, 197, 209, 229, 240, 301, 315.

construction of, 202, 205, 206, 207, 233, 240.

nature of corporation as affecting scope of, 230, 231.

theory of general corporate capacity, 340.

theory of special corporate capacity, 340.

[References are to Pages.]

PREFERRED STOCK,

- nature of, 612.
- power of corporation to issue, 551, 598, 602, 609.
- rights of holders of, in distribution of assets, 550, 554, 613, 619.
- rights of holders of, to pro rata share of new issue of stock, 592.
- when entitled to payment of dividends, 548.
- guaranteeing, 550.
- power of, to vote, 611.
- not an indebtedness of corporation, 619.

PRIVATE CORPORATIONS,

- as distinguished from public, 73.

PROMISSORY NOTES,

See **NEGOTIABLE PAPER.**

PROMOTERS,

- defined, 917, 918.
- relation between, and corporation, 903, 918, 920, 922.
- right of, to contract with corporation, 916, 929.
- right of, to compensation, 920, 928.
- liability of corporations for contracts of, 928, 929.
- liability of corporations for contracts of, in quasi-contract, 928, 929, 930, 932, 934.
- ratification by corporation of contracts of, 934, 936.
- adoption by corporation of contracts of, 932, 936.
- effect of failure of, to make full disclosure, 907, 922.
- liability of, for deception, 910, 912, 920.
- liability of, for secret profits, 916, 919.
- duties of, to associates, 915, 919.
- equivocal prospectus of, 920.
- effect of assent of corporation to transactions of, 925.
- effect of assent of dummy stockholders to transactions of, 910, 923, 927.

PROPERTY,

See **ULTRA VIRES ACQUISITION AND TRANSFER.**

- of corporation distinct from shareholders', 7, 8, 436, 513, 692.
- power of corporation to lease or sell all its, 224, 227.
- power of corporation owing public duties to alienate its, 231, 267, 296.

PROXY,

See **VOTING.**

Q

QUASI-CONTRACT,

See **ULTRA VIRES CONTRACTS; PROMOTERS.**

[References are to Pages.]

QUO WARRANTO,

when action of, lies against corporation, 58, 120, 185, 940, 948, 951.
to test right of director to office, 450.

R

REBATING,

corporate liability for, 16.

REMOVAL,

of directors, 445, 450.

S

SET-OFF,

right of, when shareholder sued on subscription, 780.
right of, when shareholder indebted to corporation, 564.

SHARES OF STOCK,

See STOCKHOLDER; TRANSFER OF STOCK; SUBSCRIPTIONS TO STOCK.

distinguished from capital stock, 106, 109, 513.

distinguished from property of corporation, 109.

distinguished from certificates for, 358, 361, 736, 738.

what represented by, 110, 608.

invalidity of, issued in excess of authorized capital, 619, 622.

right to issue, at a discount, 622, 625, 627.

right to issue, for money's worth, 627.

taxation of, 109, 113.

right of corporation to buy its own, 209, 211, 212, 214.

right of corporation to take its own, in extinguishing a debt, 214.

right of corporation to purchase, in another corporation, 215, 216, 218,
244, 245, 286.

right of corporation to take, in another corporation, for the extinguish-
ing of a debt, 216, 218.

SHERMAN ANTI-TRUST ACT,

civil liability of corporation for violation of, 702.

criminal liability of corporation for violation of, 22.

SOLE STOCKHOLDER,

right to maintain replevin to recover corporate property, 9, 10.
corporation as, 45.

SPECIAL ACT,

formation of corporations by, 114, 121.

formation of corporations by, now generally forbidden, 121.

abuses due to corporations being formed by, 114, 121.

STATE CONTROL OF CORPORATIONS,

amend, alter or repeal charter, 67, 418, 609, 611.

when reserved, 418, 421.

[*References are to Pages.*]

STOCKHOLDER,

See SUBSCRIBER; SUBSCRIPTIONS TO STOCK; SHARES OF STOCK; TRANSFER OF STOCK; CREDITORS; VOTING.

- nature of interest of a, 3, 437, 513, 586, 608, 678.
- contract as basis of creation of status as, 363.
- when subscription makes one a, 356, 360, 361.
- when books of corporation determine who is, 728, 736.
- as trustee for other stockholders, 719, 724.
- distinguished from mere subscriber, 354, 360, 364.
- damages for breach of agreement to become a, 355.
- necessity of transfer to, on corporate books, 357.
- necessity of payment to become, 363, 365, 384.
- necessity of certificate to become, 361, 736.
- powers of, 440, 444.
- validity of deed executed by all, 437.
- liability of, on shares issued at discount, 625.
- right to contract with corporation, 497, 693.
- right to prevent alienation of all corporate assets, 227, 229, 708.
- right to vote, 520, 521, 587, 713.
- right to create voting trust, 523, 531, 540.
- right to make by-laws, 539, 543.
- right to dividends, 548, 554, 563, 567, 574, 578, 587.
- right to stock dividend, 557, 563.
- right to subscribe to unissued original stock, 579.
- right to subscribe to new stock issue, 581, 588, 591.
- right to inspect corporate books and records, 592, 594.
- right to distributive share on dissolution, 587.
- right to sue on behalf of corporation,
 - must first exhaust remedy within corporation, 640, 669, 690, 701.
 - necessity of application to stockholders, 643, 647, 654, 655, 670, 672.
 - essentials of suit in equity by, 647, 653, 656, 690.
 - when Federal courts take jurisdiction of, 649, 653.
 - Federal rule in equity No. 94, now No. 27, as affecting, 655.
 - where stock of, acquired after transaction complained of, 655, 666, 673, 676, 678.
 - when application to directors unnecessary by, 655, 657, 665, 715.
 - must set out cause of action in favor of corporation, 669, 673.
 - corporation as a necessary party defendant, 673, 690, 701.
 - misconducting directors as defendants, 673.
 - must be brought in representative capacity by, 673, 704.
 - effect of acquiescence of predecessor, 673, 676.
 - effect of laches, 680, 684.
 - effect of acquiescence by plaintiff, 684.
 - effect of questionable motive, 689.
 - effect of suit brought as puppet for another corporation, 688.
 - effect of prior similar suit by another stockholder, 691, 695, 696.
 - effect of stock of plaintiff being fictitious, 628.

[References are to Pages.]

STOCKHOLDER—Continued.

- distinguished from suit brought by a stockholder on his own behalf, 694, 695, 699, 700.
- right to sue on own behalf,
 - to restrain ultra vires acts, 694, 697, 698.
 - to restrain illegal acts, 701.
 - at law, as distinguished from equity, 699.
 - when not permitted to, 700.
- relation of, to creditors, at common law, with regard to unpaid subscriptions, 823, 828.
 - with regard to stock issued for money at less than par, 830, 834, 842.
 - with regard to stock issued for property at an overvaluation, 850, 853, 858.
- relation of, to creditors, by statute, 858, 864, 865, 869, 873, 878.
- who liable as, to creditors, 882, 886, 898, 901.

SUBSCRIBER,

- distinguished from stockholder, 354, 360, 364.
- nature of contract of, 369, 377.
- right to revoke subscription, 370, 393, 396.
- necessity of issuance of stock certificate to, 360.
- necessity of payment by, 363, 365.
- liability of, to creditors, 368.
- effect of secret agreement with, 402, 405.
- effect of change in corporate enterprise on, 409, 413.
- effect of fraud upon, 421.
- effect of death or insanity of, 371.
- corporation as a, 387.
- implied agreement by, to pay for shares, 392, 396.
- power of directors to release, 394, 397.
- power of shareholders to release, 397.

SUBSCRIPTIONS TO STOCK,

- as condition precedent to corporate existence, 128.
- right of corporation to demand payment of, at par, 631.
- when conditional on all shares being subscribed for, 379, 388, 391, 395.
- payment of, 381, 384, 392, 396.
- statutory requirements as to, 382, 384, 391.
- in de facto corporations, 384, 387.
- nature of liability for, 363.
- distinguished from contract for purchase of shares, 359.
- essentials of contract of, 369, 372, 374, 379, 381.
- right to revoke, 370, 393, 396.
- effect of conditions in, 396, 398, 402, 405, 408, 632.
- effect of change in amount of capital stock on, 394.
- effect of false representations upon, 394, 421.
- effect of change in business of corporation on, 398, 408, 412, 413, 418, 421.

[References are to Pages.]

SUBSCRIPTIONS TO STOCK—*Continued.*

- effect of secret stipulation in, 402, 405.
- effect of statute of frauds on, 407.
- effect of unauthorized acts of directors on, 414, 416.

SURETY,

- power of corporation to be, 231.

T

TORT,

- liability of corporation for, 11, 14.
- liability of corporation for ultra vires, 346, 347, 352.

TRANSFER OF STOCK,

- necessity of, on corporate books, 735, 740, 747.
- right of corporation to inquire into motive for, 729.
- right of corporation to object to, because of indebtedness of stockholder, 730, 735.
- power of transferor to confer title on second transferee, where first transfer not on corporate books, 739.
- when owner estopped to deny, 757, 763, 766, 769.
- validity of restraints on, 726, 729.
- whether delivery of certificate essential to, 735, 741.
- by delivery of certificate, 736.
- equitable title under, 738, 740.
- damages for refusal to make a, 745.
- validity of unrecorded, as against attaching creditors of transferor, 752, 757.
- relation of certificate holder with blank power of attorney to transferor, 740, 755, 760.
- relation of certificate holder with blank power of attorney to corporation, 740, 755.
- effect of, upon shareholder's liability for calls, 749, 751, 752.
- effect of, upon liability of transferee for calls, 750, 751, 752.
- effect of neglect of corporation to register, on books upon shareholder's liability, 745, 748, 749.
- when corporation entitled to indemnity on, 772, 778.

TRUST DEED,

- right of corporation to enforce, in excess of its authorized powers, 290, 305.

TRUSTEE,

- corporation as, for stockholders, 8.
- power of corporation to be a, 232.

TRUST FUND,

- capital stock as a, 632, 716, 782, 788, 796, 836, 845.
- repudiation of doctrine, 789, 793, 842.

[References are to Pages.]

TRUSTS AND MONOPOLIES,

- agreement forming, 55.
- nature of, 57, 66.
- construction of powers of, 202.
- injunction by shareholder against corporation entering, 703.

U

ULTRA VIRES (IN GENERAL),

- term defined, 281, 285.
- distinguished from illegality, 281, 285.
- doctrine to be reasonably applied, 198.
- acts of directors, 459, 464, 471, 689.
- development of theory of, 241, 342.
- analogy to *de facto* doctrine, 343.

ULTRA VIRES ACQUISITION OF PROPERTY,

- effect of, 234, 237, 239, 243.
- rule that only state can object to, 238, 241, 254, 258, 308, 327.
- passing of title in, 243.
- by grant, 261.
- by devise or bequest, 246, 255, 258.
- mortmain doctrine as affecting, 257, 263, 302.
- distinction between taking and holding, 257, 261.

ULTRA VIRES TRANSFER OF PROPERTY,

- effect of, 264, 266, 268, 274.
- passing of title in, 266, 268, 271, 274.

ULTRA VIRES CONTRACTS,

- contractual liability under, where executory, 278, 283, 288, 289, 309, 337, 346.
- contractual liability under, where partially executed, 275, 278, 293, 296, 299, 303, 310.
- contractual liability under, where executed, 289, 304, 326.
- quasi-contractual liability on, 289, 293, 296, 299, 319, 322, 325, 332.
- right of rescission of, 318, 328, 331, 332.
- right of state to intervene, 308, 317, 327, 341.
- distinguished from illegal contracts, 281, 299, 302, 311, 316, 334.
- effect upon, of ratification by stockholders, 281.
- Federal or strict theory of, 296, 300, 303, 316, 323.
- liberal theory of, 304, 311, 312, 318, 323.

ULTRA VIRES TORTS,

- corporate liability for, 346, 347, 352, 353.
- ratification by stockholders of, 351.

UNDERWRITING,

- nature of agreement of, 936, 938.

[References are to Pages.]

USURY,

corporate liability for, 22.

V

VOTING,

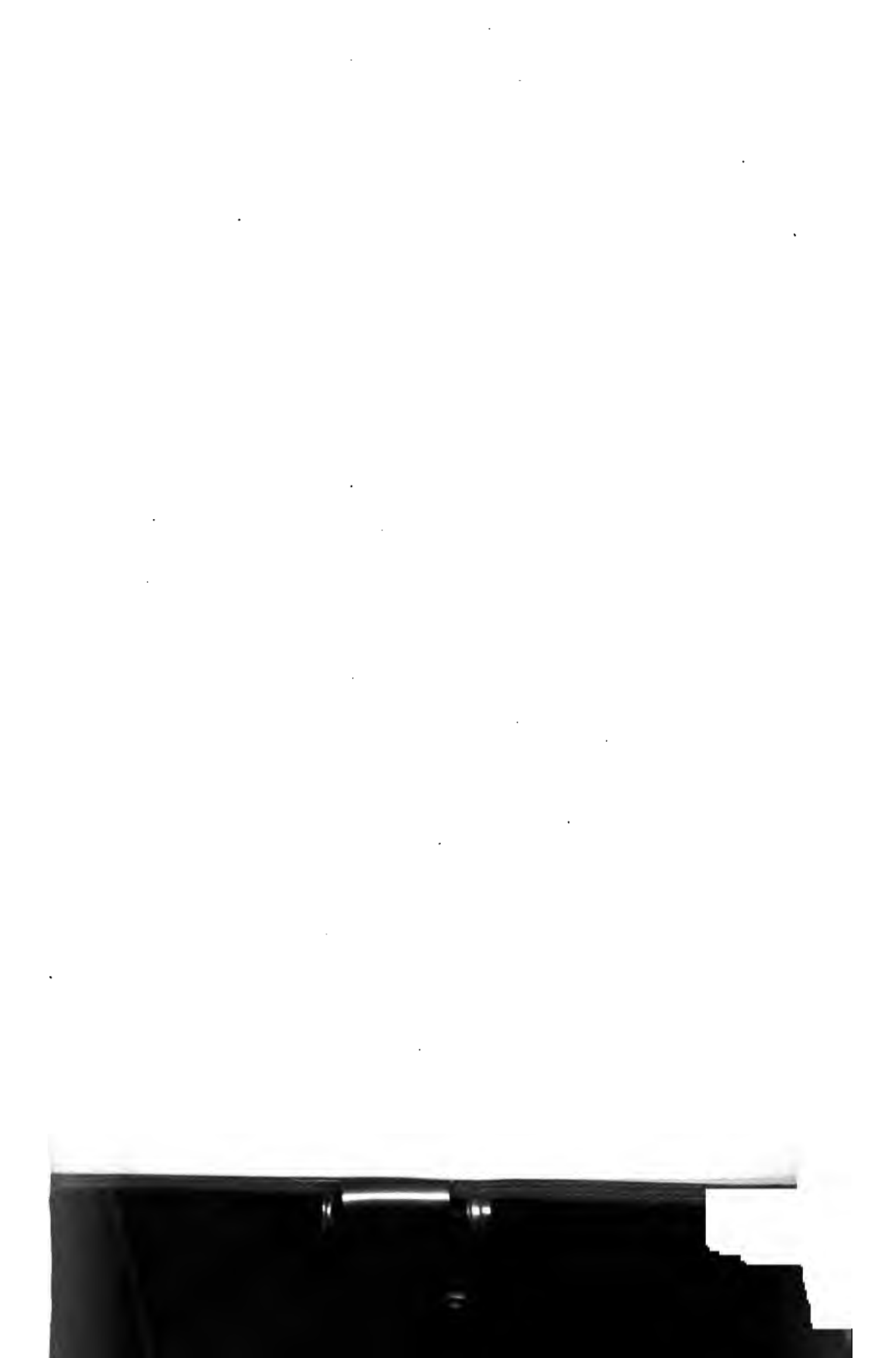
number shareholders entitled to, in, 521.
right of corporation as to, shares in another, 521.
right of, follows legal title, 522.
right of, as affected by personal interest, 521.
right of, as affected by motive, 520, 662, 713, 715, 720.
by pledgee, 522.
by personal representative, 523.
by bondholder, 523.
by proxy, 529, 531, 534.
by corporation, 719.
cumulative, 523.
trust, 523, 531, 540.
value of, 521.

W

WATERED STOCK,

when capital stock is fictitious or, 625, 627, 634, 639.
liability of holders of, 631.
whether void, 633, 639.
effect on, of honest estimate, 635.
right of shareholder to prevent issue of, 637, 639.
liability of a corporation issuing, to forfeiture of charter, 639.





CT BCD CCc
Cases on private corporations,
Stanford Law Library



3 6105 044 209 836

